A STUDY ON VALUATION OF STOCK IN NEPAL STOCK MARKET

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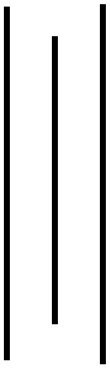

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RECOMMENDATION

This is to certify that the Thesis

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has been prepared as approved by this Department in the prescribed format of the Faculty of Management. This thesis is forwarded for examination.

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VIVA-VOCE SHEET

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And found the thesis to be the original work of the student and written according to the prescribed format. We recommend the thesis to be accepted as partial fulfillment of the requirement for the

Degree of Master's in Business Studies (M.B.S.)

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DECLARATION

I hereby declare that the work reported in this thesis entitled **"A STUDY ON VALUATION OF STOCK IN NEPAL STOCK MARKET**" submitted to Office of the Dean, Faculty of Management, Tribhuvan University, is my original work done in the form of partial fulfillment of the requirement for the Master's Degree in Business Study (M.B.S.) under the supervision of **Joginder Goet** of Shanker Dev Campus.

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Subash Shrestha
Researcher

TABLE OF CONTENTS

Acknowledgement

Table of Contents

List of Tables

List of Figures

Abbreviations

Page No.

CHAPTER – I INTRODUCTION

1.1 Background of the Study 1

1.2 Statement of the Problem 5

1.3 Objective of the Study 8

1.3 Significance of the Study 9

1.5Limitations of the Study 10

1.6 Organization of the Study 10

CHAPTER – II REVIEW OF LITERATURE

2.1 Conceptual Review 12

2.2 Review of Journals 17

2.3 Review of Previous Studies 21

2.4 Research Gap 30

CHAPTER – III RESEARCH METHODOLOGY

3.1 Research Design 31

3.2 Selections of the Sample Companies 31

3.3 Sources of Data 32

3.4 Data Collection Technique 32

3.5 Hypothesis 32

3.6 Tools of Analysis 34

3.6.1 Financial Parameters 34

3.6.2 Financial Tools 36

3.6.3 Statistical Tools 37

CHAPTER – IV DATA PRESENTATION AND ANALYSIS

4.1 Significant Trend and Development of Stock in Nepalese Security Market 39

4.1.1 Economic Liberalization and Capital Market Development 39

4.1.2 Primary Market 40

4.1.3 Secondary Market 42

4.1.4 Present Status of Stock Market in Nepal 45

4.1.5 Equity Growth and Confidence of Investors 50

4.1.6 Stock Exchange 51

4.1.7 Some important Trend in Security Market 53

4.1.8 Factor Affecting the Nepalese Stock Market 55

4.1.9 Psychology of Nepalese Stock Market 58

4.2 Risk and Return of Stock Market 60

4.2.1 Market Capitalization and NEPSE Index 62

4.2.2 Risk and Return of Banking Sectors 66

4.2.3 Risk and Return of Insurance and Finance Companies 75

4.2.4 Market Value of Banking, Insurance and Finance Companies 82

4.3 Time Series Data of Sample Companies 84

4.3.1 Time Series Data of Commercial Banks 84

4.3.2 Time Series Data of Insurance and Finance Companies 89

4.4 Major Findings of the Study 94

CHAPTER – V SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Summary 97

5.2 Conclusion 100

5.3 Recommendations 102

Bibliography

Questionnaire

LIST OF TABLES

Table No.	Title	Page No
4.1	Trends of the Primary Market	41
4.2	Trends of the Secondary Market	44
4.3	Securities Market Indicators	48
4.4	Current Stock Market Characteristics	52
4.5	Market Capitalization of Each Sector an Overall Stock Market Capitalization	63
4.6	Sector Wise Year-end Index up to 2007	64
4.7	Computation of Overall Market Return	65
4.8	Computation of Risk and Return of Banking Sector	67
4.9	Summary Tables of the Sample Companies	75
4.10	Computation of Fisk & Return of Insurance & Finance Sector	76
4.11	Summary Table of the Sample Companies of Finance and Insurance Sector	82
4.12	Time Series Data of Sample Companies of Commercial Bank form 1998-2007	85
4.13	Multiple Correlations of Commercial Banks	86
4.14	Coefficient and P-value of Five Variables	87
4.15	Time Series Data of Insurance and Finance Companies	90
4.16	Multiple Correlations of the Time Series Data	91
4.17	Coefficient and P-value of Five Variables	92

LIST OF FIGURES

Figure No.	Title	Page No
4.1	Trends of the Secondary Market	45
4.2	Securities Market Indicators	49
4.3	Market Capitalization of Each Sector an Overall Stock Market Capitalization	63
4.4	Sector Wise Year-end Index up to 2007	64
4.5	Computation of Overall Market Return	66
4.6	NEPSE Index of Banking Sector	68
4.7	NEPASE Index of Insurance and Finance Companies	77

ABBREVIATIONS

ADB	-	Asian Development Banks
BODs	-	Board of Directors
BOK	-	Bank of Kathmandu Limited
CGT	-	Capital Gain Tax
CIF	-	Citizen Investment Fund
CRR	-	Cash Reserve Ratio
EBL	-	Everest Bank Limited
FCs	-	Finance Companies
FSRs	-	Financial Sector Reforms
GDP	-	Gross Domestic Product
GDS	-	Gross Domestic Saving
GNP	-	Gross Nation Product
HBL	-	Himalayan Bank Limited
IMF	-	International Monetary Fund
NABIL	-	Nepal Arab Bank Limited
NDF	-	Nepal Development Bank
NEPSE	-	Nepal Stock Exchange Centre
NG	-	Government of Nepal
NPA	-	Non-Performing Assets
NPL	-	Non-Performing Loans

NRB	-	Nepal Rastra Bank
ROA	-	Return on Assets
SAF	-	Structural Adjustment Facility
SAP	-	Structural Adjustment Program
SCB	-	Standard Chartered Bank Limited
SEBO/N	-	Security Board of Nepal
SMC	-	Securities Marketing Centre
TU	-	Tribhuvan University

CHAPTER – I

INTRODUCTION

1.1 Background of the Study

In Nepalese context, some financial institutions involved in capital market are Nepal Rastra Bank, commercial Bank, Agriculture Development bank, Nepal Industrial Development Cooperation, Employee provident funds, citizen Investment Trust, co-operative Agencies, Rural Development Banks, Securities Board, NEPSE, Rastriaya Beema Sansthan, Insurance companies Financial Institutions, Co-operative Agencies, Non-Government organization, some Hotels, manufacturing and Trading Agencies etc. These institutions play a vital role in the development of capital market, like money market, Nepalese capital markets are also classified in organized sector and non-organized sector. Government agencies and other institutions, which are already mentioned above categorized in-organized sectors, they provide long term fund for the development of agriculture, industrial and commercial sector by investing in stock, debentures, and government bonds. Individual investors, merchants and private sectors also help for the development of capital market. Rural Areas are still dominated by unorganized sectors. It implies that mass poverty and exploitation from higher classes are still found in these areas (Bhattarai 1997:15).

The development of the economy requires the productive activities, which in turn is the result of the investment venture in productive enterprise. The establishment of these enterprises needs a huge amount of funds. There are mainly two sources of financing the productive enterprises the internal external sources. The internal financing has the limited scope because the limited resources and risk associated with the investment. So, now a days, the external financing, the method of financing an enterprise through the financial market, has become the most important and popular sours of financing for fostering the productive activities in the economy. Now, all economic units including the household and government have to rely external financing. Thus, the stock market, the most important component of the financial market (market for financing assets), is a must for the development of an economy. In

the Nepalese context, the external financing has the limited scope because of the least developed financial market in the economy. The savers and the investors are the same in the Nepalese economy, which is one of the discouraging factors for the rapid growth of investment in productive activities.

Capital market plays a vital role in new developing the nation's economy. The trading of shares of stocks takes place in the stock market. Nepal, the capital deficient economy, requires the huge amount of investment monthly in production activities for the rapid economic development. The stock market can play the vital role by encouraging and canalizing the saving to provide the entrepreneurs for investment in profitable projects in the Nepalese capital market. In the context of Nepalese capital market it is in institutional arrangements in which a number of institutional bodies like securities Board Nepal (SEBO/N) Nepal stock Exchange (NEPSE), Register of company (ROC), Shareholders association Nepal and listed companies are in existence. In Nepalese Capital market twenty-seven brokers, ten market intermediates and one organized stock exchange center are currently in operation (Bhattarai, 1997:25) Only few listed companies listed to NEPSE and most of the listed companies are in active and rarely their share is traded on the floor. Nepalese stock market is infancy stage but it is growing slowly. If we take the size of the market we can compare. It with a person suffering from a disease, due to which his height is not increasing but gaining its weight only. However there is also a marginal mental development. It is so because market is mostly concentrated over commercial banks only Nepalese capital market is very small as compared to other neighboring countries. Banks, Non-banking financial companies and insurance company occupy 90% of total market capitalization (SEBO/N, 2007:2).

The basic functions of stock market are still to provide and allocate capital funds to firms with profitable investment opportunities and to offer and avenue of liquidity for individuals to invent current income for borrow against future income and there by achieve their preferred time pattern of consumption because investing involves uncertainty, capital markets also provoke a means for transferring risk among the parties to their transactions.

The stock market and economic activates move in similar cyclical patterns. In the Nepalese economy the demand and supply of funds for investment in productive enterprise is low due to the absence of mechanism for transferring risk which, in turn, may be attributed to the absence of well developed stock market.

As a first financial institution in Nepal, Tejarath was established in 1993 B.S. from government side. But it only provides loan in favor of government employees with minimum interest rate. Although Nepal Bank limited was established in 1994 B.S. it could not generate enough funds for business and industrial purpose. It only provide short-term loan for individual and business institutions by pledging as collateral. After the establishment of Nepal Rastra Bank in 2013 B.S. as a central Bank of Nepal, it was founded as a base of capital market. It was also authorized to issue government securities (like government bond's treasury bills, National saving certificates etc) to collect the national debt. Without participating in private sectors, capital market could not be developed appropriately. Considering this, Nepal industrial development corporation (NIDC) was established in 2016 B.S. The basic function of NIDC was to encourage private sector for industrial activities. It also helps for the improvement and modernization of private sectors by providing economic and technical subsides. The contribution of employee provident funds (2019), Rastriaya Beema sanstahan and Agriculture Development Bank (2024) cannot be able to minimize the development of security and sale of security. However, it could not help the institutional development of security exchange because the

basic objective of these institutions was not related to security exchange activates. Thus, to provide the investment opportunities to potential investors, collection and mobilization of funds for industrial purpose, the need of organized institution has been felt at that time. Considering this, for the development of well functioning secondary market, security exchange centre was established in 2033 B.S. Though it was established in 2033 B.S. it was permitted to work as a security Act in 2040 B.S. The main purpose of the establishment of SEC is to accelerate the pace of industrial growth in the national economy and also to create security exchange activities.

Nepal Stock Exchange Ltd (NEPSE) is the only stock exchange in the country. The Government of Nepal, Nepal Rastra Bank owns Nepal Industrial development corporation and its members and their ownership; in the exchange are 52.5%, 39.72%, 7.04% and 0.69% respectively, security exchange Act, securities regulation and NEPSE's own Memorandum and Articles of Association have empowered NEPSE to promulgate various By-LAWS,1996 and membership; of stock exchange and transition bye laws, 1998 and has been taking responsibilities of making the securities transition and their clearing and settlement activities more clearly and fair (Annual Report, SEBO/N, 2000/01).

The concept of stock market in Nepal is very new. It is still in infancy stage though Nepal Bank Ltd and Biratnagar Jute Mill Ltd began it with the flotation of Shares in 1937 under the Company Act 1936. At that time the participation on the ownership structure of the corporate sector was restricted mostly to the Rana family. Consequently, the expansion of the capital market to the desired level had been restricted. No significant attempt had been made in four five-year plans to reform the capital market. The establishment of Securities Exchange Center (SEC) in 1976 was the first and most important attempt made by the government to develop the stock market. Initially the SEC served to promote the primary as well as secondary market for government and corporate securities from fiscal year 1984/85. Although the growth of stock market is high relative to the growth of the economy, the share of corporate sector in the national economy is still very low due to the negligible size of the corporate sector. The incorporation of the securities Board Nepal (SEBO/N) under the Security Exchange Act, 1993 and conversion of the SEC into the Nepal stock exchange (NEPSE) under the government policy of capital market reform has greatly contributed to the development of primary as well as secondary market of the corporate securities were observed immediately after the incorporation of SEBO/N as NEPSE for one year only. This has positive and immediate impact on the primary market. But after a year, again downward trend in the primary as well as secondary market is observed and this phenomenon has been continuing till now.

1.4 Statement of the Problem

The stage of development of capital market in any country and its effective growth is depended upon the aggregate economic condition, saving and investment opportunity, effective role of private sector etc. Involvement of private sector in the capital market helps reinforcing the market would ultimately yield better results.

The development of corporate culture is the most for the development of capital market. Actually corporate culture is the sole of corporate business. It depends on saving of investor investment and attitude towards taking risk.

The founder and manger of organization, associated businessman and regulatory bodies and their attitudes to public investors are related to the development of corporate culture of capital market. So, our capital market is assumed to be small and in a developing stage to protect the investment in favor of investors and also for the sound development of market, the regulatory system and legal infrastructure are also essential as in other parts of financial market. Capital market is not able to contribute in economy in comparison to developed countries because it could not introduce variability in resource mobilization, market liquidity and security instrument etc.

Actually, the problem of the Nepalese stock market have not been diagnosed and identified so the policy makers are unable to make the appropriate policy for the development of the stock market. Most of the government efforts for the development of the stock market since 1976 have poorly contributed to the stock market development, (securities exchange center was established in 1976), only in the early nineties, the government policies to reform the capital market under the Extended Structural Adjustment Program (ESAP) have left some positive impact for the development of the stock market. However, this also has not become sustainable because of the lack of the policy. The stock value and liquidity in the stock market increases immediately after the introduction of modern system of trading and conversion of SEC into the Nepal Stock Exchange. This attracted the general public to invest, their savings in the stocks which causes the stock value rise further. The hike and the more liquidity and the secondary market left positive and immediate impact

on the capital mobilization in the economy. However, this upward movement in the stock value and the liquidity in the secondary market did not remain for long. The highly overvalued stock began to decrease and then value of all stock fall simultaneously. This downward trend of the stock value continued and caused the liquidity of the secondary market to fall and then mainly the under subscription of the public issue (lower supply of funds). Other than banking sector was realized on primary market which, in turn, lead to lower demand for funds form the public. These show that the primary market is positively and highly elastic with stock value and the liquidity in the secondary market (Bhattarai, 1987:29). Thus the equilibrium of the supply and demand for funds from the general public is set to lower level than the most harmful signals to the stock market and the economy as a whole.

Nepalese capital market is very small in comparison with other efficient developed stock market. There are few numbers of brokers, limited no of listed companies, very few transactions and most importantly investors are unknown about the pros and consequences of the stock market, while capital market may damage the national economy badly and if one the investors' confidence were lost it would be very difficult to bring it in original condition.

The behavior of the stock value shows the mis-valuation of the stock value in the secondary market. The price and earnings information was not made available timely to the investors. The investors could not identify the good and bad stocks. The only speculative behavior of the investors regarding the future stock value lead to set the stock value in the market. The value of some stocks, which have sustained less for long period, reached to the peak level while that of some stock with sustained profit could not increase. Thus, the lack of value judgments to determine the stock value is the serious problem of the Nepalese stock market. This happens due to the inability of the regulatory bodies of the stock market to regulate the market mechanism and failure to win the faith of the investors. Thus problem can be solved only when the real determinates of stock value are diagnosed and identified. The research studies on this issue are not available in the Nepalese stock market .The present study is carried

out to diagnose and identify the current problem of the Nepalese stock market. The following problems are seen in Nepalese capital market and stock market.

a. Low price and low trading volumes of companies have directly related to market value of firm. Due to lack of sound dividend policy, most of the companies have not been able to maximize the value of a firm in secondary market.
b. Earning, Dividend payout ratio and growth rate have significant impact in market equity of the companies. But financial need of the companies does not match with these variables in secondary market.
c. Marketability, liquidity and diversification of investment are other problem exists in stock market. If market price and number of share traded will go down, it directly affects liquidity in marketability of stock.
d. The rate of return and holding period have significant role to market value of firm, the average rate of return of overall market was 125.95 percent in year 1994 A.D. Due to decreasing trend of market index, market returns till 1998 were less than zero. Due to the increase of market index since 1999 the average return of overall market was seen positive till 2000. Again due to the continuous fall of market index, the average rate of return was continuously fallen up to 2005.
e. Lack of sufficient information disseminates to investor and lack of transparency has another problem that exists in Nepalese stock market. It manly affects financial position of the company market information system and corporate governance of the companies.
f. Regarding with various problem in capital market as well as stock market, the study deal only stock market behaviors by analyzing return, risk, market value of firms and other significant qualitative variable that directly affects value of a firm and also stock price.

1.3 Objective of the Study

The main objectives of the study are as following:

1. To highlight the trends and significant development of stock in Nepalese security market.
2. To analyze the sensitivity of securities (especially banking, financing and insurance sectors) and compare with market return.
3. To examine the relationship between market capitalization's with other independent variables such as earning per share, dividend per share, price earning ratio, dividend yield, earning yield and return on equity.
4. To recommend the improvement of stock value in stock market in Nepal on the basis of findings.

1.4 Significance of the Study

The term 'Security Market' refers to the buyer and seller of security as also structure of comprising sale and resale of companies' securities (Bhusan, 1991:35). By providing efficient market mechanism for collection and mobilizations of funds, stock market has a significant role to accelerate the pace of industrial growth in the national economy and also to create the concept of stock exchange activities. In Nepalese context stock market has recent phenomenon than in developed countries. After establishing the securities Board in 1994 A.D it took place in modernization. Lack of appropriate information dissemination system absence of professional brokers, rigid roller and regulation, small value of trade and declining transition, infant state of investment banking and lack of investors' consciousness are main problem in stock market. Due to in adequate infrastructure and limited activities of security exchange counter, Nepalese market could not contribute in economy as compared to developed countries. Regarding various problems this study is only concerned with stock market performance, relationships of risk and return of securities, quantitative determinant factors of market capitalization and also other factors of stock market.

The descriptive and diagnostic approaches are used for this purpose. In the descriptive part, it is concerned with significant trends and development of stock in Nepalese security stock market, securities development indicators, present status of stock market in Nepal etc. To find out risk and return relationship, the diagnostic approaches are used. The calculation of risk and return of any investment are highly significant in any organization. In the capital market, risk involved in any types of investment in securities can be measured in terms of co-efficient of characteristic in line as developed by William Sharp but this study uses simple model of risk and return models (Dividend Yield Plus Capital Gain). Cross sectionals analysis are highly significant to find out relevant and irrelevant factors related to market capitalization (Value of firm) by using this dynamic model it helps to predict and change in a firm systematic risk and its expected return simultaneously. Regarding this, the study also tries to highlight some determinant factors to market price of share and stock market.

1.5 Limitations of the Study

As each and every study have its limitations. We have limited research and it may be difficult to explore researchers to find out new aspect.

Reliability of statistical tools used and lack of research experience are the major limitation and some other limitation can be enlisted as follows.

1. This research study is mainly based on secondary data, which have been collected from books, financial statement and report of the SEBO/N, Nepal stock exchange and options of respondents. The study covers the information of only few fiscal years' data. The study has to be done depending largely on secondary data and company's website.
2. This study is so limited form the point of view of submission on partial fulfillment of the requirement for the Master Degree in Business Study.
3. The study is fully based on the students' financial resources and is to be completed within the limited time. Further, the study is not a final study on the subject.
4. It is also limited to analyze these problems that directly affect a stock price and also stock market.

5. The study mainly, concerned with banking (commercial banks), finance and insurance sectors, which are listed in stock exchange limited.

1.7 Organization of the Study

The study has been organized into five chapters, each chapter deals with the specific aspects of the study, which is as follows: -

Chapter I: Introduction
Chapter II: Review of Literature
Chapter III: Research Methodology
Chapter IV: Data Presentation and Analysis
Chapter V: Summary, Conclusion and Recommendations.

The first chapter deals with the introduction consisting, background of the study, statement of the problem, objective of the study, significance of study limitations of the study, and organization of the study.

The second chapter is mainly focused with literature review that includes a discussion on the conceptual framework on fund mobilization and review of previous studies i.e. books, journals, articles dissertation etc.

The third chapter describes the research methodology used to conduct the present research. It deals with research design, sources of data, data processing procedures, population and sample, period of the study method of analysis and financial and statistical tools.

The fourth chapter deals with presentation, analyze and interpretation of relevant data through definite courses of research methodology using various financial and statistical tools and at the end of chapter major finding of the study have been presented.

The fifth chapter is the last part of study, which is related to summary, conclusion and recommendations of the study and at the end of the study bibliography and appendices have been included.

CHAPTER - II

REVIEW OF LITERATURE

The second chapter consists of relevant review of literatures, which is very important as it provides valuable inputs to this study. Only by knowing what others have said, one can be realistic to make the study more useful and relevant. In this chapter an attempt is made to review some of the comprehensive and relevant literature on the valuation of stock in stock market. In this regard, basic academic course books on finance, recent published books specially related to the topic, some of the major research based journals and the related studies are reviewed. The available literature relating to the field of this study and conceptual thoughts are presented below:

2.1 Conceptual Review

The primary motive for buying a stock is to result it subsequently a higher price. In many case dividend will be expected too. Dividend and price changes are the principal ingredients in which investors regard as return on yield. The existence of well functioning secondly market where investor came together to trade existing securities, assured the purchase of primary securities that they can quickly sell them to securities, if the need areas.The Nepalese capital market has been passing through the transition phase over the past few decades after since independence. There are various inconsistencies and hindrances exited on the way of functioning of market. Not only that institutional both bottlenecks are hampering the growth of capital, but at times, the existing imperfect national characteristics phenomenon deeply noted in socio economic system hears undermine the proper trading in securities market. The arbitrarily quoting of stock in securities market. The arbitrarily question of stock price without fundamental and technical justification made securities market not to look after the protection of investors (Shrestha, 2004:35).

So far as the securities (stock) market is concerned, it is an important constitute of capital market. It has a wide term embracing the buyers and self of securities and resale's of corporate securities. Stock market is a financial market, which probably

has the greatest glamour, and is perhaps the lest understood. Some observers consider it as a legalized heaven for gambling and money investor consider stock market inviting as a game in which consider stock market inviting as a game in which the sole purpose is picking winners. Having said this, stock market. Investment can be both rewarding and fun so as long as sufficient time is given to appreciate its many characteristics (James and peter, 1995).

Investment decision in the stock market is a function of the providing market size and return to capital. It is important to predict the course of national economy because economic activity affects the corporate profits, investors' attitudes and expenditures and ultimately security prices. The key for analysis overall economic activity, the behavior of stock price of stock market, linkage between stock market and economic activities is critical ((Richard, 1998:720).

Generally, demand and supply of stock market is influenced by rational and irrational factors. The change of single factor elicits conflict relating from different sector's such if demand of share increase, market price of stock is high and vice versa. In the absence of active market price changes are less frequent but more stable due to efficient operation of secondary market. Stock market is also capable of handling regular, transaction and testing heavies' obscurities. These transactions (purchase and sales of securities of stock) are also judiciously recorded by companies site. Those who prospect higher values, which facilitate the financing and growth.

Stock market price itself on being a barometer of the future rather than thermometer of the resent, but in the absence of other information, investors perhaps tend to base the validation of companies. excessively in recent past performance (Winfield and Curry, 1995:6).

The true investor is interested to seek a good rte of return or a relatively lag period of times. The true speculator or seek a good rate of return of a relatively lag period of

time. Thus, the same stock can be purchased as a speculator in investment depends on the motivational purchaser (Donald and Jordan, 1998,:729).

Like as liquidity, market efficiency is another most profound idea to affect the investment decision process in security markets, mainly in equity markets. This means that efficiency priced markets in which the prices of security do not depart for any length of time from the justified economic values. The security value (estimated economic values) in market is determined by investment expectation about earnings risk and so on. In an efficient market, if the efficient market value is going to be changed as rational inventors, they react with new information and set revised estimated economic value quickly and accurately. Thus, securities are efficiently priced on a continues basis, obviously, ad positively the stock market has an efficient and significant implication for investors. The word efficiency has been used in security market in various logically distinct concepts. Efficiency is one of profound ideas that affect the investment decision process. Markets efficiency may be defined in different context of areas, for instance, organizational efficiency, investment efficiency, allocation efficiency, informational efficiency, operation efficiency etc. Efficiently means efficiently priced markets in which price of security doesn't depart form justified economic values for securities which are determined by investor's future expectation about risk earnings and so on. If market price of shares are deviated from justified economic values, as rational investors of efficient security markets, he tries to adjust the estimated economic values according to new information arises in an efficient market price. Thus, securities are efficiently priced on a continuous basis. FM, which has a significant implication for investors in stock market, would directly affect the investment process sand investment decision.

Information is the centre issue of efficient market concept. To estimate the economic value of stock, all inventors are used, and reasonably obtain available information. It consists of both known information and belief about the future. So "Efficient" refers to quick and accurate reflection of information in prices" (John, 1994:423). Efficient market concept also assures that availability of information must be reflected in

prices. It includes past and current information, as well as announced information hasn't transpired. Further more information that can be reasonably inferred is also assured and reflected in prices. These types of information have quickly and accurately transferred nature i.e. the security prices quickly adjusts such information. Thus, the efficiency of security prices depends on the speed of price adjustment to any available information. The more speed of adjustment are the more efficient the prices.

An efficient market (FM) is defined as one in which the price of security fully reflects all known information quickly and accurately (John, 1994:425).

The security price must be reflected by the available information as a price conscious investor's security prices and return both are determined in the stock market. Prices are principal components of return. quickly and accurately dissemination of information is another concept that the investors will assimilate all information into prices in making buy and sale decision, So, current stock prices incorporated available information. According to Reilly in buying and selling process of securities, investors concern their nature and are also aware of information adjustment". Efficient market is that, where large number of knowledgeable and profit maximizing independent buyers and sellers, new information is generated randomly and investors adjust the information rapidly (Sharpe, 1998:15). They are also highlighted that, in efficient market, it is only possible to earn normal profits and normal rate of return in their investment.

An efficient market is one where a security's current price gives the best estimate of its time watch. In an efficient market, there are higher free Launches, non- expensive dinner. It is not possible to systematical gain or lose profits from trading on the available public information (Western and Copland: 1995: 731).

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in making buying and sale decision. So current stock prices incorporate available information. According to Reilly in buying and selling process of securities investor concern their nature and are also aware of information adjustment." Efficient market is that where large number of knowledgeable and profit maximizing independent buyers and sellers, new information ids generated randomly and investors adjust the information rapidly (Sharpe, 1998:15). They are also highlighted that, in efficient market, it is only possible to earn normal profits and normal rate of return in their investment.

An efficient market is one where a security's current price gives the best estimate of its time watch. In an efficient market, there are higher free launches, non expensive dinner. It is not possible to systematically gain or lose profit from trading on the available public information (Weston and Copeland: 1995:731).

All these definitions are related to information efficiency. Finally, we can say that information dissemination in market plays a significant role to estimate the market price obscurities. Rapid and accurate adjustment of information system has signified more efficient market and only possible to earn normal profits and normal gain. The subject of market affiance has been much coerced area of the studying recent time. The informational efficient markets are not only related to informational efficiency but also allocation, operational efficiency etc. Allocation efficiency signifies, that rate of return adjusted the risk that are equated the margin for all investors. At time minimum transferred lost of investment funds refers operationally efficiency.

2.2 Review of Journals

So far there are no such advanced and research based journals in the field of finance in Nepal. There are very limited numbers of journals associated in the subject of management and it is further hard to find any article in the subject matter of finance. In Nepalese context, there are limited studies available with stock market and most of the studies are related to the theoretical concepts. So, some foreign well -known journals are taken into considerations, which are spread out all over the world.

There is growing empirical evidence that multiple factors are cross- sectionals correlated with average returns into he united state. Measured over long period time period, small stocks earn higher average return then large stocks(Bang,1981) Fama French(1994) show that value of stock with high book-to-market(B/M), earning to price(E/P); on cash flow to price out perform growth stocks with low B/M, E/P, or C/P. Moreover, sock with high return over the past three months to one year continues to out perform stocks with poor prior performance (Jagadesh and Titman, 1993). The evidence that the data is also compensated for in average return is wakes (Fama and French (1992), Kothari, Shakhen and Stoan(1995).

These data provide unavailable information which helps to understand long term histories of capital markets. If it relies on the historical data as the basis for estimate for long term market growth, there is no reason to look at U.S. data only. This is why, our paper paints an broad pictures of the performance of global stock market over more than 75 years of a turbulent country of financial market (Zorin and Goetman, 1999:957). The basic idea of this study is global capital market, which has been systematically subjected to dramatic changes over this century. The U.S. stock markets expect that the other markets of world have been closed and suspended due to financial crisis wars, and expropriation political upheavals. The U.S capital appreciation return is 4.3%. The U.S. stocks are in rather expectation than other markets because other markets return are only 0.8% median return. These results suggest that the large equity premium obtained in the U.S. is at least partly to the results of conditioning may also create times variation in expected returns; for instance, we expect that market may do well exhibit more mean reversion than other because periods of large losses must be followed by periods of up winnings. The study also treats the hypothetical performance of a globally diversified investment. The performance of globally diversified portfolios is around 4.0% which is the closest to the U.S. equities. It should be clear the that we fail to account for the looser' and well as the winner in the global equity markets, we are providing a biased view of the history which ignores important information about actual investment risk (Zorin and Goetman: 1999: 976).

Brennan and Henry have conducted a study about international portfolio invest flows in journal of finance. In the study they construct a portfolio between foreign as well as domestic market and find out that domestic investors are able to get quick information than foreign investors and take enough benefits by it. According to them, the article develops a model of international equity portfolio investment flow based on difference in international endowments between foreign and domestic investors. It is shown that when domestic investors posses cumulative information advantage over foreign investors periods when the return on foreign assets is high and to sell when the return is low.

In Nepalese context, there is little study available about stock market behaviour in small capital markets. Out them, this study mainly concerns with the stock market behavior in a small market' by Radhe Shyam Pradhan in 1993 and The Dividend policy and value of firm in small stock market conducted by Kamal Das Manandhar in 2004.

The study about stock market behavior in a small capital market: in a case of Nepal has conducted by Radhe Shyam Pradhan in 1993. This study helps to provide at least some insight into stock market behavior in Nepalese content by concerning listed and traded shares in secondary market. The purpose of this study is to address the stock market equity, market value to book value, price earning and dividends with liquidity, leverage profitability assets turn over and interest coverage. To find out the above objective, this study periods of 1986 to 1990. According to him, this paper is based pooled cross section analysis of 55 observations. Data could not be obtained on contacting the individual enterprises as they traded them confidential.

Due to initial and UN established stage of stock market, there is not system yet to compile and publish stock market data on regular bases. There is no database, which make it difficult to carry on any research in Nepalese stock market. Considering the study period of 1986 to 1990, usable data could be obtained for 17 enterprises (pradhan, 1993:216). These enterprises are in different sectors such as manufacturing, banking, trading, hotels, insurance etc. In this study, he constructs a three different

level of portfolios of sample securities (small, intermediate, and large.) according to market equity, market value to book value price earnings and dividend per share to market price per share, dividend per share to earning per share and analyze liquidity, leverage, earnings and coverage of each portfolio in terms of largest and smaller and also average ratios are computed.

The result indicate that larger stock have longer price earning ratios larger ratio of market value to book value of equity, lower liquidity, lower profitability, and smaller dividends. Price earnings ratio and dividend are more variable for smaller stocks, whereas market value to book value of equity is more variable for larger stock. Larger stock also has higher leverage, lower assets turnover and lower interest coverage but there are more variables for smaller stocks than for larger stocks. Stock with larger market value to book value of equity has larger price earning ratio and lower dividends. These stocks also have lower liquidity, higher leverage, lower profitability, lower turnover and lower interest coverage. However, there are more variable for assets with smaller price earning ratio. Stock paying higher dividends have higher liquidity, low leverage, high earnings, higher turnover and high interest coverage, liquidity and leverage ration are more variable for the stock paying lower dividends while earning assets turnover and interest coverage more variable for the stock paying higher dividends (Pradhan, 1993:216).

Dividend policy and value of the firm in small stock market" in the context of Nepal has conducted by Kamal Das Manandhar in 2004 in managerial dynamics. The basic objective of this study is to find out the financial variables that are related to market equity. "The study is aimed at identifying some of the significant variables that are significant to the value of firm. The analysis, to some extent, helped to understand the dividend policy of the sample companies and their effects on market value of the firm as represented by market capitalization and this understanding helps to know the relevancy and irrelevancy of dividend policy on market capitalization in the stock market in Nepal. At the time of research, he has found the following problems in stock market and dividends practices.

1. Most companies are underrating the expectation of investors and thereby resulting how marketability of share and trading floor of stock exchanges.
2. Majority of the companies are declaring dividends less than risk free rate and market risk premium.
3. The relationship between the earning, dividends pay out and growth of the expansion program of the companies does not match with financial needs of companies.
4. Companies do not follow on sound dividend policy. These are the main causes that are related to the low price of stock and low volume in stock market.

To find the above objective, this study has included the financial data that are related to secondary market of top ten companies of the year 2003/04 on the basis of traded amount. According to this study, the model development to test the hypothesis between dependent and independent variables. So the independent variables are dividend per share, earnings per share, return on equity, dividend by closing market price and market equity is dependent on variables. At last, this study found out that the financial variable taken under study to understand the dividend policy followed are DPS, EPS, P/E, ROE an IP through not exhaustive, based on analysis it is found that DPS, ROE and D/P ration have significant impact whereas ROE and P/E have found no significant impact on market value.

2.3 Review of Previous Studies

As we know the behavioral of stock market plays a significant role in the development of capital market as well as the economic development of the country and to find out the realistic theoretical model to test the appropriate hypothesis in stock market. However there are no any specific research have been performed since the establishment of capital market in Nepal. Some studies have been conducted as a thesis for the partial fulfillment of master degree in T.U. whose some section are related to the research topic. Regarding with various unpublished dissertation this study is mainly concerned with recent papers about behavioral aspects of stock market. In this regard different theses were reviewed.

Khatiwada (1999) conducted the study on "securities investment in Nepal by using four year data form 1993 to 1996. He tries to show how the security market has been functioning by analyzing the same stock market indicator. And also he tries to present issue market and stock market performance in theoretical base such as legal aspects of secondary market, primary market and also money market. At the time of research he sets the following objectives in order to achieve the basic aim.

1. To assess the new issue market performance
2. To present the comparative analysis of money market, in the face of new issue market.
3. To analyze the stock market performance
4. To measure the stock market in terms of size liquidity and concentration.
5. To suggest the remedial measures for the importance of security markets.

The study period is too short. It is not possible to give a true picture about securities markets. At the time of research he used only simple average; percentage has been practiced for logistic presentation of the market performance. In research design, he explains As a title of this study cannot be the descriptive analysis of stock market, this study has no being on the exploratory, experimental, survey or experimental, approach to the research. It deals with the secondary markets on the basis of available information. In order to justify the data gathering as to fixed deposits, interest rate and dividend pay off, graphic methods have also been embarrassed. But it failed to describe from the behavior side and based on explanatory and descriptive analysis of the recent information and data. Only shown in the graphic presentation of data with legal controversy, the objective of the research has not been completed, there is essential of diagnostic analysis of market mechanism because it helps to give true picture about studies, specify about objective is another problem. The broad objectives are not able to properly analyze.

Jeet Bahadur Sapkota (2000) entitles "Risk and return in commercial bank in Nepal. The basic aim of this study is to analyze risk return of securities of listed companies of Nepal stock exchange limited. The main target of this study is potential investor who

wants to invest in security but repel by imaginary and an unreal risk. So, the study will be more significant for exploring and increasing stock investment." The basic objective of this study is to describe risk, return, and volatility of stock and some relevant and irrelevant factors, which are very important to make decision in stock investment. It also observes the unseen problems facing by individual investors.

Risk and return analysis is an important concept of investment decision process. It helps to make a good investment opportunity in stock market as well as new issue market. Basically, this study analyses risk and return of commercial banks which are listed and traded in NEPSE. The study period was 2049/50 to 2055/56 (or after liberalization policy has been launched). And data are collected from secondary sources, banks official, SEBO/N NEPSE, brokers etc. The tools for analysis are market price of stock and dividends and also expected return, standard deviation, covariance, and coefficient of variance betas etc. it is based on hypothetical data and more analytical and empirical types of research rather than descriptive.

Although this study helps to analyze risk and return concept with considering risk, however, it ignores financial risk and return of related companies. Without considering financial risk and return only, market return could not be able to make optimal investment decision.

This paper also doesn't appropriately observe the unseen problems facing by individual investors. Regarding with various problems in stock investment in security market, the study is able to conclude following findings.

1. It enables the investors to put the return as they expect and the risk they may take into better prospective.
2. Nepalese economy is in emerging stage but due to lack of the appropriate information and other knowledge, Nepalese private investors cannot analyze the securities as well as market properly.
3. Banking industry is the biggest one in terms of market capitalization and turnover and return for common stock of commercial banking sectors are more parallels with market return.

4. This study has also found risky and higher return projects by analyzing coefficient of variance, beta, (less volatile and higher volatile market). The portfolio approach of investment is better way to win the stock market investment.

Gopal Prasad Bhatta (2005) entitledAssessment of the performance of listed companies in Nepal. Bhatta's study in performance of listed companies is based on 10 listed company's data from 1999 to 2004. One of the major objectives that concern with this research topic is 'to analyze the performance of listed companies in terms of risk and return i.e. expected rate of return and company specific risk, required rate of return and internal rate of return, systematic risk and diversification of risk through portfolio context.

Bhatta addressed the following findings in risk return behavior form the analysis of different stocks. "A highly significant positive correlation has been addressed between risk and return character of the company. Investors expect higher returns for those stocks that associate higher risk. Nepalese capital market is not efficient one. So the stock price does contain all the information relating to market and company itself. Neither investors analyze the overall relevant information of the stocks nor does the member of stock exchange try to disseminate the information. So the market return and risk both may not represent reality. However, the analysis based in the available information shows high priced stocks such as BBC, NIV, NIC, has higher beta risk than others, these companies this requires higher returns to satisfy the investors for their risk premium.

Investors in Nepal have not yet practiced to invest in portfolio of securities. An analysis of the two securities portfolio shows that the risk can be totally minimizes if the correlation is perfectly negative. In this situation, the risk can totally be diversified, but when there is perfectly positive correlation between the returns of the two securities, the risk is undiversifiable. The analysis shows some has negative

correlation and some has positive one. Negative correlation between securities returns is preferred for diversification of risk.

On the basis of findings Bhatta concluded: "An analysis of risk and return shows that many companies have higher unsystematic or specific risk. There is a need of expert institution that will provide constancy services to the investors to maximize their wealth through rational investment decision.

Lastly, Bhatta recommended the following points to improve the market efficiency:

1. Developed institutions to consult investors for risk minimization.
2. Establish an information channel in Nepal stock exchange and
3. Market proper amendment on trading rules.

To some extent Bhatta focused in the analysis of risk and return in common stock investment. But due to so many other aspects of analysis investor cannot easily assess the results. Indeed, study did not focus the view point of investors rather it concentrates the companies and stock market. However, this study also explores some dimensions for further research in this subject.

Aryal, (2003) conducted study on "The general behaviour of stock market". Using serial correlation analysis and runs test on daily closing prices of 21 stocks during 13 Jan, 2001 to 13sepetember, 2001conducted is conducted with the following objectives.

1. To discuss theoretical movements of stock market price changes of an individual common stock as a whole.
2. To develop the empirical probability distribution of successive price changes of an individual common stocks markets as whole.
3. To examine whether the successive price changes of stock market are independent of each other or not.

The main findings of the study are;

1. On the basis of the run test and serial correlation, it seems that the independent assumption of random walk model in stock market prices is rejected by collected sample data of 221 companies, at least as a description of price behavior in Nepal stock exchange. The share price changes are dependent on each other.
2. The random walk model of security speculative price behavior has been refuted at least in the Nepalese context, which clarifies that the knowledge of the past becomes useful in predicting the future movements of stock market prices.
3. The securities in the past were incorrectly prices either over or under valued as actual market prices of securities.
4. There exists frequent persistence than reaction in the general stock market climate because of the investors' irrational behavior that causes the irrationals movement of prices of stock.
5. The general stock market of Nepal for the initial period appeared to be inefficient in incorporating the possible appearances of information into the successive prices changes. Therefore, the investing publics are not aware of the information available publicly, appropriately in adjusting with the actual market price.

Dhakal (2003) studied on dividend and stock price behavior which was carried out by the data for 16 enterprises from 1998 to 2002. This study used simultaneous equation model as developed by Friend and Puckett (1964).

The main objectives of the study were as follows:

1. To test the difference between dividend per share and shares prices.
2. To determine the impact of dividend policy on share prices.
3. To identify whether it is possible to increase the market value of the stock changing dividend policy or payout ratio.

The main findings of the study are as follows:

1. The difference between dividend per share and stock price is positive in the sample companies.
2. Dividend per share affects the share prices variedly in different sectors.

3. Changing the dividend policy or dividend per share might help to increase the market price of share.
4. The difference between stock prices and lagged earning ratio is negative.

Shrestha (2004) studied on "Share Prices Behavior in Nepal" was conducted with the following objectives:

1. To examine the efficiency of stock market of Nepal.
2. To determine whether the sequence of price changes are consistent with changes of the series of random number expected under the independent process.
3. To determine the efficiency of the stock market through the theoretical model of "efficient market hypothesis" in the stock market.

He examined daily closing prices of 30 stocks during the period from 13 Jan, 1994 to mid July 1998 by means of serial correlation and runs tests found that the successive prices changes are dependent.

The main finding of the study is:

1. The prices changes of the past and present can be very helpful to forecast future price changes. Therefore there exits the sufficient amount of opportunities for the sophisticated investors.
2. When days increase the mean value of serial correlation of coefficient is lower, that indicates that the past price changes may have low power to predict the future price changes in the long run.
3. The price changes in the present and future stock market may not be independent of the price changes in the past and present respectively.
4. There exist no profitable trading rules to make greater profit than they would make under the naïve buy and hold strategy in their speculation through the information of past price changes.
5. Nepal stock exchange is not efficient in pricing shares.

Paudyal, (2005) studied on "A study on share price movements of joint venture commercial banks in Nepal" is undertaken by using financial and statistical tools (standard deviation, correlation, beta, t-test etc) the major objectives of he study are:

1. To examine Nepal stock exchange market and to judge whether the market shares of different banking indicators (book value per shares and major financial ratio) explain the sharer price movements.
2. To analyze the scenario why the shear of selected banks emerge as blue chips to the potential investors and to make a conclusion the basis of the financial ratios analysis.
3. To examine how risky the investment in commercial banks share are.

The major findings are:

1. The market shares of these banks do not capture the market share and the growth rates of different banking indicators used.
2. The ordinary least square equation of book value per share on market value per share. Share reveals that the independent variable doesn't fully explain the dependent variable on the basis of the above mentioned two points. Nepal stock exchange operates in a weak form of efficient market hypothesis, indicating that the market price move randomly.
3. Having good track record of the financial position, the market potential investors buy the shares of joint venture commercial banks. Therefore, the shares of joint venture commercial banks. Therefore the shares of joint venture commercial banks emerge as blue chips in the Nepalese stock market.
4. The beta coefficient, which measures the risky ness of individual security in relative term, suggests that none of shares of eight sampled banks are risky. The shares of publicly quoted joint venture commercial banks are less risky as compared to other average stocks traded in the stock exchange.

Dahal (2006) studied on "Stock market behavior of listed joint venture company" describes the Nepalese stock market as follows:

The main objectives of this study are to study, examine and analyze the stock market behavior, the specific objectives are:

1. To study and analyze stock price trend and volume of stock traded on the secondary market.
2. To study and analyze the rate of listing of new companies and maintenance of listed company in Nepal stock exchange ltd.
3. To study and analyze the investors vies regarding the decision on stock investment.
4. To study examine the singling factors impact on stock price with the help of NEPSE index.

Dahal said that stock market is the backbone of investment sector of the country. Nepal stock exchange is not providing facilities for investors such as general awareness about investment, investment procedure for general public and movement of stock trend in different periods and their cause are not explained. Most of investors are complaining that the market makers, brokers, and NEPSE s staffs are making coalition for fraudulent activities towards investors. So NEPSE should clear this type of charge for the development of stock market.

2.4 Research Gap

Very few studies have been conducted in the field of valuation of stock price n Nepalese security market. The government policy to reform capital market under the extended structural program and modern system of open cry out had significantly positive impact on stock market development. After the restoration of democracy the government has launched linearization policy, which build the expectation of the establishment of multinational companies but unfortunately lack of proper implementation, it is seems useless in stock market development. So such studies have needed for promoting the stock market time to time since share price is the crucial phenomenon in the stock market and there is an increasing trend in the common investment.

Present study tries to analysis valuation of stock price in Nepalese security market by applying various facts using secondary data. It can be very useful or important in this area. Thus, present study will be fruitful to those interested person, parties, scholars, professor, students businessmen and government for academically as well as policy perspective. Hope this study will help to others in future in the related field.

CHAPTER - III

RESEARCH METHODOLOGY

Two types of research has been employed in this study mainly descriptive and diagnostic Research. Descriptive analysis incorporated and highlights the significant trend and development of stock market, securities market indicator etc. And in the other sides, Diagnostic analysis mainly highlights to find out Risk and return of overall market, each sector and also individual companies. Cross sectional behavior of time series data are also done to find out dependent and independent variables by using statistical tools of multiple regressions.

3.1 Research Design

Two types of research have been employed in this study mainly descriptive and diagnostic research. Descriptive analysis incorporated and highlights the significant trend and development of stock market, securities market indicator etc. And in the others sides, diagnostic analysis mainly highlights to find out sensitivity of overall market, each sector and also individual companies cross sectional behavior of time series data will be done to find out dependent and independent variables by using statistical tools of multiple regressions.

3.2 Selections of the Sample Companies

The research is based on secondary source of data. The listed companies in the secondary market already reached to 135 by the year-end 20067/08. However, the time frame of the study includes 1998-2008. Therefore the researcher has taken only the date. The listed companies are selected on the basis of their availability of relevant data and the frequency of transaction on NEPSE floor during that period since the period has shown that the Banking industry, financial and insurance companies were heavily traded during the period, the researcher will therefore, cover most of them while selecting the companies for the sample. Eleven samples have been selected. The selected companies are seven from commercial banks(standard Charter Bank limited, Bank of Katmandu, Himalayan Bank limited, Nabil Bank limited, Nepal SBI ltd,

Nepal Bangladesh Bank and Everest Bank ltd) two finances companies (Katmandu finance ltd and Annapurna Finance co. ltd) and two insurance companies(premier Insurance company ltd). The sampling procedures also consider financial status size, maturity and market value of listed company.

3.3 Sources of Data

To conduct any research, data collection is a major task. This research is mainly based on the secondary sources of data and information. Major secondary sources are as follows:

1. Annual report of sample companies
2. Quarterly bank and financial institution statistics published by Nepal Rastra Bank.
3. Economic survey published by Nepal Government, Ministry of finance.
4. Previous Research studies and Articles on the subject.
5. Various IMF, World Bank, UN Reports.

3.4 Data Collection Technique

Study is based on secondary data. For the secondary data and information, publication of Nepal Rastra Bank, annual reports of sample companies, various publications of Nepal Rastra Bank. Apart from these various books, a journal, seminars papers available in the library and relevant articles from the website has been used.

3.5 Hypothesis

Testing of hypothesis is one of the most important aspects of the theory of decision-making. It consists of decision rules required for drawing probabilistic inferences about the population parameter is the same as before, as claimed or has changed.

The hypothesis has set to achieve the objective of this research. T-test of single mean, different mean, and multiple regressions has been employed for this purpose. The hypothesis would be:

1. H_{01}: The average return of individual companies is equal to overall market return i.e. there is no significant difference between an average return of sample

companies, and also select oral return (such as Banking, insurance and finance companies Ltd.) in 95% significant level. The T- static of single mean and different mean T-test are used.

a) T-statistical of Single Mean

The single mean test has used to compare return of individual companies and overall market return.

The "T" statistic under the null hypothesis is = $\frac{\bar{R} - \mu}{\frac{s}{\sqrt{n}}} \approx t_{n-1}$

Where,

$\bar{R}$ = return of sample companies

μ = Overall Market Return

S = $\sqrt{\frac{1}{n-1}\Sigma(R-\bar{R})^2}$

b) T- Statistics of Different Mean

To test the hypothesis between market return and return of each sector, T- Statistic between different mean are used.

The 'T' Statistics under null hypothesis is:

$$S = \frac{\bar{R}_j - \bar{R}_m}{\sqrt{S^2(\frac{1}{n_1} + \frac{1}{n_2})}} \approx t_{n1} + t_n - 2$$

Where,

Rj = Return of each sector of sectoral return

Rm = Overall Market Return.

S^2 = $1\frac{1}{n1+n2-2}[\Sigma\Sigma(R-Rj)^2 + \Sigma(\bar{R}m - \bar{R}m)^2$

2) H_{02}: EPS, DPS, P/E Multiple dividend and earning yield and also return an equity are independent factor of market capitalization.

While testing these hypotheses, market capitalization is assumed dependent variable and other financial variables are independent variables. But individual hypothesis would not be tested for this purpose.

The multiple regression equation has used for this purpose. By using the sophisticated tools for analysis like SPSS (Statistical Package for the Social Science), MS- Excel are used to develop regression model and to test the hypothesis of time series data.

3.6 Tools of Analysis

3.6.1 Financial Parameters

a) Earning Per Share

It is an earnings made by single unit of a share. It measures the profit available to equity holders on a per share basis i.e. the amount that they can get on every share hold. It is calculated by dividing the profit available to the share holders by number of outstanding share. The profit available to share holder is by net profit after taxes and preferences dividend. Thus,

$$EPS = \frac{\text{Profit after Tax}}{\text{No of Common Shares Outstanding}}$$

b) Dividend per Share

The Market Value of share is dependent on the dividend distributed to equity holders. A part of net profit belonging to0 equity share holder is retained in the business and balance is paid to them as dividend. The share basis is DPS, i.e.

$$DPS = \frac{\text{Earning Per Share to Shareholders}}{\text{No of Share outstanding}}$$

Total Dividend = Cash Dividend + % of Stock Dividend × Next Year MPS.

c) Price Earning Ratio

P/E ratio is the ratio of current stock Price to last year earning per share. The P/E ratio tells us how much stock purchaser must pay per Rs. of earning that the firm generates. It has been calculated as:

$$\text{Price Earning Ratio} = \frac{\text{Market Value Per share}}{\text{Earning per Share}}$$

d) Dividend Yield

Dividend yield is the ratio of common stock it is measured as dividend per share by market price per share it tells us how much a common stock holder received per share it has been calculated as.

$$\text{Dividend Yield} = \frac{\text{Dividend Per Share}}{\text{Market Price Per Share}}$$

d) Earning Yield

The inverse of P/E ratio is called an earning yield and it is measured as earning per share to market price per share.

$$\text{Earning Yield} = \frac{\text{Earning Per Share}}{\text{MarketPrice Per Share}}$$

e) Return on Equity (ROE)

Return is the income received on an investment ROE is the ratio of net income to common equity. It measures the rate of return on common stock holder's investment it is calculated as net profit after tax by net worth.

$$\text{ROE} = \frac{\text{Net profit after Tax}}{\text{NetWorth}}$$

f) Market Value to Book Value Ratio (MV/ BV)

Market valley to book value is the ratio of current stock market price to its book value. It gives indication of how inventors regard the company it helps to analyze the company past performance a future prospects.

$$\text{MV/ BV} = \frac{\text{Market Value Per Share}}{\text{Book Value Per Share}}$$

g) Market Capitalization

Market Capitalization is the value of the firm. Generally market capitalization is equal to the number of share outstanding multiplied by share prices if other things are

constant large market capitalization means smaller stock return, higher liquidity and marketability.

Market Capitalization = Market Price of Share × Listed Number of Share of Each Company

3.6.2 Financial Tools

a) Return

An adequate measurement of security return constitutes regular income and income from price changes. This type of measurement is called Holding Period Yield (HPY).

Symbolically:

$$\text{HPY} = \frac{\text{Cashpayment Received}}{\text{Purchased Price}} + \frac{\text{Price Changed over the Time Period}}{\text{Purchase Price}}$$

$$\text{HPY} = \frac{P_1 - P_{T-1} + D_T}{P_{T-1}} \times 100$$

Where,

Pt = price change over the 'T' period

Pt -1 = price change over the't-1' period i.e. price of last year.

Dt = dividend of't' year

HPY = Holding period yield.

$$\text{Market Return} = \frac{\text{MI t - MIt -1}}{\text{MI}_{t-1}} \times 100$$

Where,

MI_t = Overall Market Index of't' period.

MI_{t-1} = Overall Market Index of't-1' period

Similarly, Return of insurance and finance sector would be calculated as: -0

$$\text{Return} = \frac{IF_t - IF_{t-1}}{IF_{t-1}} \times 100$$

IF_t = market Index of Insurance and finance sector of't' period.

IF_{t-1} = Market Index of Insurance and finance sector of't-1' period.

Like wise banking sectors:

$$\text{Return} = \frac{B_t - B_{t-1}}{B_{t-1}} \times 100$$

3.6.3 Statistical Tools

a) Standard Deviation

Standard deviation is usually denoted by small sigma (σ). It is defined as positive square root of the arithmetic mean of the square of the deviation from their arithmetic mean. It is measured an absolute term of dispersion depending upon unit of measurements.

$$\sigma = \sqrt{\frac{1}{n}\Sigma(R - \bar{R})^2}$$

b) Coefficient of Variation

To compare more than two assets, coefficient of frequency variation is used. It is relative measurement of dispersion based on standard deviation. Coefficient of variation is given by following formula.

$$\text{C.V.} = \frac{\sigma}{\bar{R}}$$

Where,

$\sigma = \text{Standard deveiation}$

$\bar{R} = \text{Average ofreturn}$

It is percentage of variation mean, standard deviation, being considered as the total variation in the mean. Smaller C.V. represents mare homogenous or uniform and less variable as compare to greater c.v. To compare different companies risk standard deviation and co-efficient of variation has been employed for this study.

c) Arithmetic Mean

Arithmetic mean of the given set of observations is their sum divided by the number of observations. In general if X1, X2,……X5 are the given 'n' observations then their arithmetic mean, usually denoted by is X given by

$$\bar{X} = \frac{\Sigma x}{n}$$

Where,

$\Sigma x = \text{Sum of observation}$

N = No of observation

To calculate average return of different companies as well as overall market, the arithmetic mean has been employed.

d) Correlation

Correlation analysis establishes the closeness of relationship between the two and more variables. It measures the degree of relationship or association between variables

e) Regression

It establishes the nature of relationship between two or more variables and then estimates the unknown variables on the basis of other known variables.

$Y = a + bX_1 + bX_2 + bX_3 + ...$

CHAPTER - IV

DATA PRESENTATION AND ANALYSIS

This chapter deals with the presentation, analysis and interpretation of relevant data of sampled companies, which were collected from various sources, are changed into an understandable presentation using financial as well as statistical tools mentioned in the previous chapter i.e., Research methodology. This chapter is the heart of this study. This chapter will be of great relevance for this study, as all the findings, conclusions and recommendations are going to be derived from the calculations done in this section. The data analysis and presentations is the core of this study. Which consists of three-sub chapter i.e. Significant trend and development of stock in Nepalese security Market, Risk and Return of Stock market, market value of insurance, finance and banking sectors. Basically, Descriptive data are used to present and analysis the significant trends and development of stock in Nepalese security. In diagnostic analysis, the hypothesis concerning the return and risk of overall market and individual companies, time series data of insurance, finance and banking sectors.

4.1 Significant Trend and Development of Stock in Nepalese Security Market

4.1.1 Economic Liberalization and Capital Market Development

As a precondition to economic liberalization, the industrial Enterprise Act was enacted n 1982 and foreign Investment and Technology Transfer Act came into existence since 1983. Since 1985, Nepal has been following liberal economic policy. In its first stage of implementation, banking and financial sector was liberalized a policy to invite foreigners to invest jointly with the domestic investors in banking and financial sector was introduced. Finance companies Act, 1986 was also enacted with a view to provide non banking services to the people in order to promote their economic benefit in general through institutionalized investment. According, many banks and finance companies were incorporated in private sector and listed in the securities exchange center. Nepal Rastra Bank liberalized of interest rate and endeavored to reform and strengthens the financial sector by implementing various prudential financial norms like income recognition, loan classification, maintenance of adequate loan loss

provision reserve and capital adequacy ratio and liquidity position of the banks and finance companies. The industrial policy of 1988 introduced various reforms in order to encourage the establishment of corporate enterprise and guaranteed the non-nationalization of private sector industrial organizations.

In August 1988, Nepal was hard hit by major earthquake resulting in considerable loss of lives and properties. Nepal-India trade and Transit Treaty came to an end on March 1989 and the country underwent more than a year long trade impasse with India which caused temporary set back to the capital market too. Most of the trade-points with India were closed down and because of the short supply of fuel and other essential industrial inputs; the operation of the most of industries was disrupted. After the restoration of multiparty democracy in 1990 and resumption of the Trade and Transit settlement with India in its status quo ante, new democratic constitution was enacted, which enshrined in its directive principles the provision conducive to the private sector growth. The multiparty election took place in April 1991 and the elected government while taking the steering of the economy realized the need to the reform the financial sector and develops capital market along with the economic liberalization in the country for private sector growth. Towards this move, more joint venture companies were opened in the country and the citizen investment Trust was established as a pioneering market institution in the capital market.

4.1.2 Primary Market

Before the establishment of the securities Exchange Center (SEC) there was no any institutional arrangement to undertake new issue and manage the sales of the shares and debentures of the corporate bodies. A public limited company could make public offering according to the provision of the company Act 1964 when SEC came into existence; it started managing new issues of shares and debentures according to the guidelines for new issues and sales management 2043(1986). It used to charge commission for its service to the issuing company varying form minimum 1.35 percent to maximum of 2.0 percent depending on the amount of new issue. A lower amount of transaction would attract a higher rate of commission and vice-versa.

Therefore the issuing company had to pay a commission of 2.0 percent for the management of new issue and sales services to SEC for an amount up to Rs. 2.5 million. The rate of commission for a new issue of Rs. 10 million and above was 1.35 percent. At present, the rate of commission ranges from 1.5 percent to 2.5 percent depending upon the value of securities sold. The issue managers who arrange the sale of securities charge commission to the issuing company at the rate of 2.5 percent of the value of the sold securities up to Rs. 2.5 million. If the value of the issue is more than Rs 10 million, the rate of commission is Rs 1.5 percent.

Table 4.1

Trends of the Primary Market

	Headings	Fiscal Year						
		2002/03	2003/04	2004/05	2005/06	2006/07	First 9 months	
							2006/07	2007/08
1	Issue Approval	717.2	1555.1	853.8	1547.8	1270.3	578.4	1537.8
	(a) Ordinary Share	268.5	528.7	551.5	755.0	300.9	27.5	334.4
	(b) Rights Share	365.8	387.9	162.2	429.9	669.4	250.9	1003.4
	Preferential Share	-	140.0	-	-	-	-	-
	(c) Debenture	-	360.0	-	300.0	300.0	300.0	200.0
	(d) Mutual Fund	-	-	100.0	-	-	-	-
	(e) Citizens Plans	82.9	138.5	40.1	62.9	45.5	-	-
2	No. of Companies making public issues	9	16	17	16	12	6	23

Source: - Economic Survey, fiscal year 2007/08

In the first 9 months of FY 2006/07, 26 corporate entities have been authorized to mobilize capital form the primary stock market for a total amount of Rs. 1537 million by issuing stock of ordinary and right shares and debentures. Such authorized amount is higher by 165.9 percent compared to the same period of FY 2006/07. In the same period of last FY, there were 6 entries which were authorized to mobilize capital of Rs. 578.4 million through ordinary and preferential share and mutual fund.

4.1.3 Secondary Market

Trading on the floor of the NEPSE is restricted to listed corporate securities and government bonds. Companies established under company act 1964 must be listed in stock exchange Ltd. Number of listed companies was 62 in the initial month of floor trading on NEPSE, then this number increased by listing of additional companies. The number of listing companies is increasing trend. The trends of group wise listed companies are increasing. The number of listed companies in finance group has increased at higher rate, than that of other sectors. The higher number of listed companies in finance groups implies the well management; facilities provided top investors, effective securities to the investors.

Securities Exchange Act 1983 made it obligatory to trade the securities through the recognized Exchange Center or through their licensed brokers. Therefore the securities Exchange center opened its floor for secondary trading of corporate shares in November 1984. Before this, the SEC was restricted to trading of Government Bonds. At present 23 member and 9 markets have been operating on the trading floor. The rate of brokerage on equity transaction varies from 1 percent to 1.5 percent depending upon the volume of trade. Higher the amount of transaction lower is the percentage of commission. The seller and the buyer both the parties have to pay the commission to the broker. However, it takes a very long period of around two months to get securities and registered in the name of the buyer.

In mid-.July 1986, there had been a total of 16 listed companies with paid up share capital of Rs. 341 million. The market capitalization of listed shares on that date and annual turnover for the FY 1985/86 amounted to Rs 548 million and Rs 10.1 million respectively. However, the security market started growing continuously thereafter and in 1990 the number of listed companies rose to 41, the paid up value of listed shares increased to Rs. 789 million and the market capitalization at mid July reached to Rs 1775 million, which is larger by more that three times to that of 1986. The total turnover of FY 1989/90 was Rs 25.3 million. At the earlier stages of growth the secondary market of securities in Nepal was very weak.

Along with the formation of security exchange Board; Nepal Government converted the securities Exchange Center Ltd. into Nepal Stock Exchange Ltd. (NEPSE) in 1994 with a view to reform the capital market. It is a non-profit making organization operating under securities Exchange Act 1983. Brokers and market makers operate on the trading floor as per the security Exchange Act rules and bylaws of NEPSE. Nepal stock Exchange started its operation on 13 January 1994 through its licensed members.

The security Board was constituted on 1993 under section 1 of the securities Exchanges Act 1983. Its main objective is to provide essential policy direction fro t he systematic and regular exchange of securities and develop competitive stock exchange is a trading institution, whereas a security Board is the regulatory board. Before the Board came into existence, the securities Exchange center carried on both the functions. Though any corporate body is desired to carry out the transaction of securities can submit application to the Board for obtaining the license. Till now, Nepal Stock Exchange Ltd, alone is representing the securities market in the country.

In the first 9 months of FY 2006/07 cash transactions in the Stock Exchange decreased by 52 percent totaling Rs. 1833.6 million with 5,893,450 shares changing hands in comparison to 13.582 million shares worth Rs. 3798.1 million transferred during the same period of FY 2005/06

Number of transactions is decreased by 13.66 percent in the first 9 months of FY 2006/07 to total 71,777 as compared to 83,135 transactions in the corresponding period of the previous fiscal year.

Table 4.2

Trends of the Secondary Market

Heading	Fiscal Year						
	2002/03	2003/04	2004/05	2005/06	2006/07	First 9 months	
						2006/07	2007/08
Value of shares traded	2344.21	1540.6	575.8	2144.3	4507.7	3798.1	1833.6
No. of Shares	4989	6005	2428	6468	18434	13582	5809.34

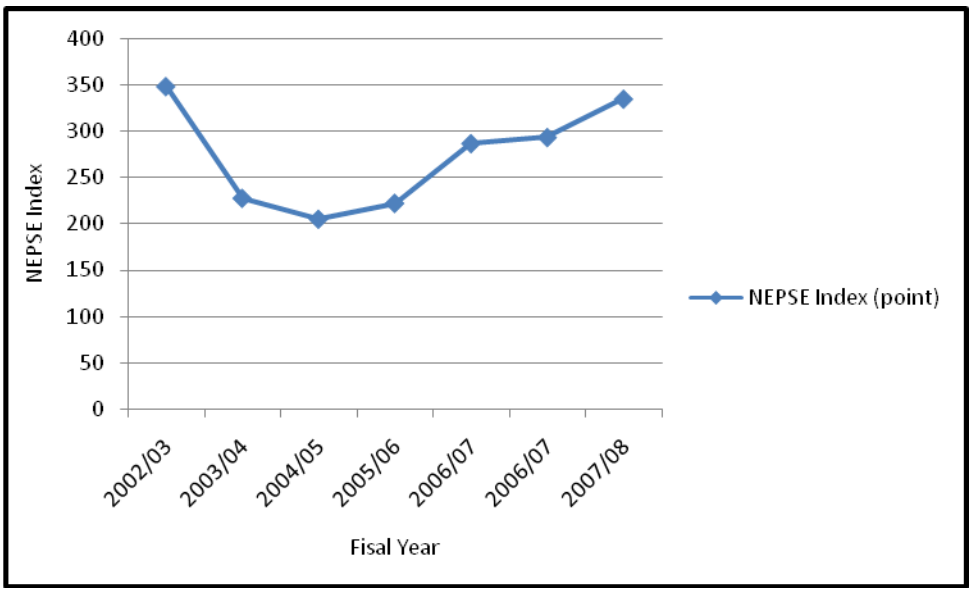
Transactions (in 'ooo')							
Transactions (No)	46095	42028	69163	85533	106246	83135	71777
Market capitalization	46349.4	34703.8	35240.4	41424.8	61365.9	62567.9	79471.3
Traded value as a percent of market capitalization	5.06	4.44	1.63	5.18	7.34	6.07	2.66
Market capitalization as a percent of GDP	11.78	8.56	8.09	8.77	12.17#	12.41	-
Paid-up value of listed stocks	8165.2	9685.0	1256.0	13404.9	16771.9	16647.0	18643.0
No. of listed entities	115	96	108	114	125	123	128
No. of Transacted companies	67	69	81	92	102	87	83
NEPSE Index (point)	348.40	227.50	204.86	222.04	286.67	293.26	334.77

Percentage computed on the basis of estimated GDP

Source: - Economic Survey, fiscal year 2007/08

Figure 4.1

Trends of the Secondary Market



With the addition of 3 corporate entities during the first 9 months of FY 2007/08 number of such entities listed in the stock exchange has totaled 135. The number of such listed entities was 128 during the corresponding period of FY 2006/07. In the first 9 months of FY 2007/08 market capitalization increased by 29.5 percent and reached to Rs. 79.47 billion compared to Rs. 61.37 billion during the corresponding period of FY 2006/07

4.1.4 Present Status of Stock Market in Nepal

Equity market has shown impressive recovery form the sharp fall in 1994 with the lag effect elongated till late 1998. At present, it has been performing more strongly than in the earlier years. The improvement in the equity market has been attributed to factors including good prospect of corporate earnings and broader household participation in the stock market. Investors not only rely on the statement of the brokers, but they also have a concern over the financial information of the concerned company. Therefore, the shares of companies with better prospect of dividend, capital increment and growth have normally higher prices in the stock market. Recent rise in equity prices can also be attributed to the gradual fall in the bank deposit interest rates causing

excess liquidity in the market. Investors without any credible investment opportunity have diverted their resources towards the stock market. At present, the stock market in Nepal has witnessed its strength surprisingly, and this has raised hopes for sustained growth of corporate undertakings.

Stock market in Nepal has been growing gradually both in terms of turnover as well as the capital investment. From 16 listed companies in 1986 they grew to 110 in 2000 and 115 and declined in the year 2002 to 96 and rose at the end of 2003 reached to 108 companies. During this period, their paid up capital surged up from Rs 341 million to Rs 12.56 billion. Number of listed companies increased by sevenfold, whereas the paid up capital went up 28 times. Market capitalization of listed shares has been rising continuously, except with a few cases of volatility. It has reached Rs 35.24 billion in 2003 from Rs 548 million in 1986. The ratio of market capitalization to paid up value increased form 1.6 times in 1986 to 5.9 times in 2000 and 2.8 times at the end of 2003. Though the annual turnover is much volatile it has reached to the highest level of Rs 2.3 billion in 2001 from Rs 10.1 million in 1986. The details of Nepal Stock Exchange is shown in the below table.

Securities Exchange Ordinance, 2005, has been effective since September 23, 2005 to make securities market regulations standard, credible competitive and transparent. The ordinance was necessary to implement the Corporate the Financial Governance Project assisted by Asian Development Bank to improve the security market.

To implement the Securities Exchange Ordinance 2006, drafting of necessary regulations is underway. The “Nepal Securities Exchange Board Management and Operation Regulation” has been submitted to Ministry of Finance for its approval. In the same ways, the drafts of “Regulations for the permission for the operation of stock”, “Regulation for the securities business” and “Securities listing and issuance Regulation” have been prepared.

During the first 9 months of FY 2006/07 Secondary Market Management of Government Bonds Regulation 2006 and Secondary Market Transaction of

Government Bond Regulation, 2006 have been made effective for the purpose of managing transactions of Government Bonds through Stock Exchange.

For the capacity building of Securities Board, the Office of Company Registrar and for the modernization of Stock Exchange, the Corporate and Financial Government project is in under implementation. The following activities have been completed under the project up to the 13th April, 2007.

1. In order for establishing electronic transaction system in Nepal Stock Exchange, Proposal have been invited from service providers and the process of selection has begun. And to increase professionalism of Nepal Stock Exchange, "Securities Exchange Market Government Report" has been prepared.
2. Preliminary draft of Request for Proposal has been prepared to establish Management information system in Securities Exchange Board (SEB), Nepal
3. A study is the process to evaluate the received proposal to establish the management information system in the office of Company Registry.

To enhance institutional governance in Nepal, Securities Exchange Board, Nepal has published the proceeding of the seminar on "Corporate Governance: Principles and Practices". The Board has also organized awareness programs in collaboration with Institute of Chartered Accountants and Nepal Banners' Association.

Table 4.3

Securities Market Indicators

Market Indicator	Fiscal Year									
	1997/98	1998/99	1999/00	2000/01	2001/02	2002/03	2003/04	2004/05	2005/06	2006/07
Number of public Issue	5	12	5	9	9	16	17	14	14	29
Total amount of Public Issue (Rs. In million)	332.20	463.36	258.00	630.31	717.20	1555.11	854.42	1027.50	1626.82	2443.28
Total Number of listed Companies	95	101	107	110	115	96	108	114	125	135
Paid-up Value of listed securities (Rs, in million)	85193	90107	105632	114057	124971	122685	159958	13404.90	16771.84	20008.55
Number of Listed Securities (‘000’)	416.23	202.61	1499.98	1157.03	2344.16	1540.63	575.80	161141	194673	227040
Annual Turnover (Rs.in million)	9.30	4.09	23.12	15.75	28.71	15.91	4.58	2144.27	4507.68	3451.43
Market Day	239	237	231	240	231	246	238	243	236	228
Number of Company Traded	67	68	69	69	67	69	81	92	102	110
Number of Shares Traded. (‘000)	9443	1195	4857	7674	4989	6005	2428	6468.18	18433.55	12221.93
number of transaction	12428	15483	15814	29136	460095	42028	69163	85533	106246	97374
Market Capitalization (Rs. In million)	12698.0	14289.0	23508.0	43123.3	46349.4	34703.9	35240.4	41424.77	61365.89	96813.74
% of Turnover on Market Capitalization	3.28	1.42	6.38	2.68	5.06	4.44	1.63	5.18	7.35	3.56
% of market Capitalization of Nominal GDP at Market price	4.71	4.93	7.12	11.77	11.78	5.58	8.22	8.77	12.06*	17.35#
NEPSE Index (point)	176.31	163.35	216.92	360.70	348.43	227.54	204.86	222.04	286.67	386.83

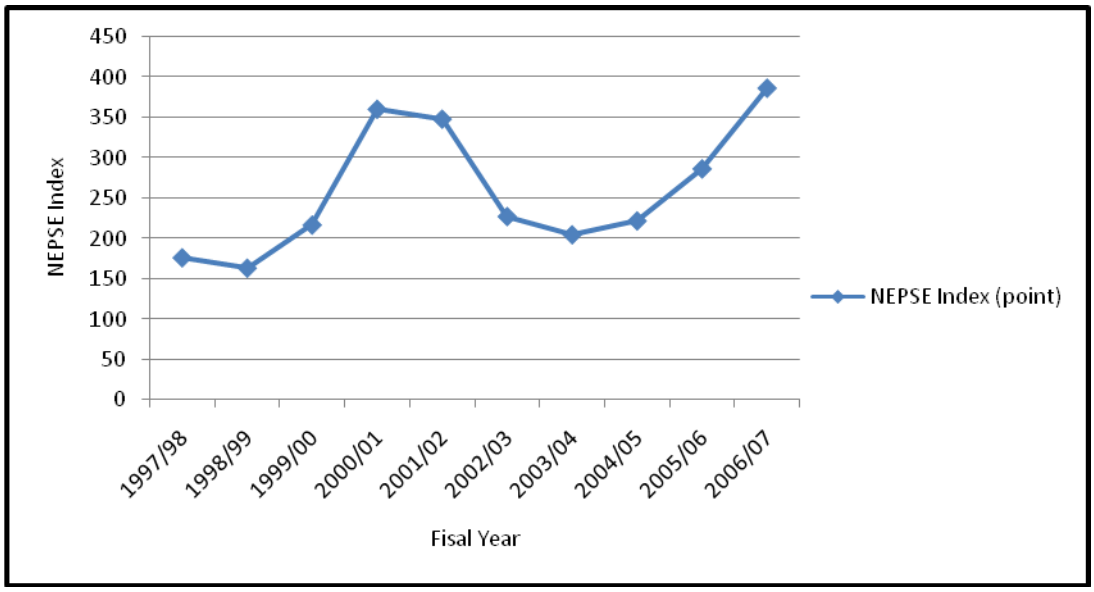
*Based on revised estimated of GDP

Based on preliminary estimate of GDP

Source: Security Board Annual Report, 2006/07

Figure 4.2

Securities Market Indicators



There was a bearish tendency in stock market since 1999. Share price of Most of the companies had gone down up to 2004. The NEPSE Index since 1999 to 2002 raised and since 2002 onwards it is in declining position except F/Y 2006/07. As compared to the preceding year market capitalization went up to Rs 96813.74 billion at mid July 2008 whereas paid capital had gone to Rs 20008.55 million. The paid up capital and market capitalization of the previous year were Rs 16771.84 million and Rs 61365.89 million respectively. The NEPSE Index moved up from 227.54 in 2006 to 386.83 at mid July 2008

The data for the 2007/08 reveals that Commercial banks occupy the topmost position in terms of annual turnover, market capitalization and NEPSE Index. Finance and Insurance sector occupy second rank in terms of Market capitalization, Annual turnover and NEPSE Index. Manufacturing and processing companies occupies third rank in terms of Annual turnover but in terms of Market capitalization other companies occupied third rank. Charts of sectors wise listed

companies, paid up value, annual turnover, market capitalization, Amount of public issue approval, Number of public issue approval.

Perfect market requires that all information concerning future risks and returns of securities are readily available to all investors. As there exists various market imperfections, relevant information are not easily available to the investors. They are often published in national daily, but most of the information is highly exaggerated and not reliable. Because of the lack of technical knowledge, majority of the investors is unable to analyze the available information. As such a single buyer and seller can affect the price of securities. Despite right from 2006, SEBO/N drafted the Securities Board of Nepal Regulation, Stock Exchange Regulation, Broker/Dealer Regulation and the Securities Registration Regulation for the implementation of the new Securities Act, 2006. in light of completion of legal arrangements to trade government bonds in the stock exchange, SEBO/N initiated the process of providing license for stock brokers and market makers for the trading of bonds.

4.1.5 Equity Growth and Confidence of Investors

The development of equity culture in Nepal was almost nil before 1985. Most of the investors were not aware of the benefits and risks associated with the equity investment. Because of the policy of economic liberalization followed by the government, many corporate under takings were encouraged to be established in private sector. At present, some of the companies are performing very well and distributing handsome rates of dividends to shareholders. This had attracted the people to diversify their savings into equity investment. The investors confidence was further boosted by police of the government to invite foreign jointly investment in various sectors of the economy. Altogether, 638 public limited companies were registered in private sector during 1993-97 including 30 companies in tourism sector, out of which only 42 companies floated their shares for public subscription in the capital market. The government started the process

of privatization since 1992. During the period 1992-94 ten corporations were privatized. Again in 1995-96, additional six corporations were privatized including the partial privatization of Nepal Bank Ltd. After the adoption of economic liberalization programmed, the number of financial institutions grew from 95 to 135 during 1998-2008.

For the effective and efficient investment decision on securities, 23 License members, 9 issue managers and 1 security Dealers have been actively working in the stock market. The number of listed companies has been increasing every year and number of actively participating companies in the security market has increased by more than two folds. Investments in the shares of many new companies were likely to earn high dividend. All of the above activities helped to raise the confidence of financial sector as well as the investors.

4.1.6 Stock Exchange

Nepal Stock Exchange Ltd. (NEPSE) is the only exchange in the country. The Govt.of Nepal, Nepal Rastra Bank, Nepal Industrial Development corporation and its members and their ownership in the exchange are 52.55%, 39.72% owns it, 7.04% and 0.69% respectively.

Securities Exchange Act, Securities Exchange Regulation, and NEPSE's own Memorandum and Articles of Association have empowered NEPSE to promulgate various Byelaws. Accordingly under the provision of section 35 subsection (2) of the securities Exchange Act, NEPSE has made securities Listing Bye-laws, 1996, and Membership of stock Exchange and transaction Bye-Laws 1998 and has been taking responsibility of making the securities transactions and their clearing and settlement activities more orderly and fair.

Nepal Stock Exchange Market Ltd, during the first the nine months of FY 2007/08 contributed Rs. 22.58 million to the government treasury by collecting capital gain

tax from the stock trading. Such collection was Rs. 34.21 million during the same period of FY 2006/07.

During the first 9 months of FY 2007/08 Nepal Stock Exchange Market Ltd. has also classified 56 of the 128 listed companies a 'A' class according to the Securities Listing Regulations, 1998. Out of 128 companies listed during the corresponding period of FY 2006/07 companies enlisted as class 'A' was limited to 48.

Table 4.4

Current Stock Market Characteristics

Sector	Listed Companies%	Paid up value	Annual Turnover	Market Cap %
Commercial Bank	11.11	42.60	78.12	70.46
Development Banks	5.93	4.08	2.40	1.63
Finance Co.	37.44	12.82	8.86	5.17
Insurance Co	11.11	6.28	3.76	5.12
Hotels	2.96	7.76	0.57	2.42
Mfg. and Process Co	21.48	13.78	0.50	5.65
Trading	5.93	0.38	0.46	0.78
Others	4.44	12.30	5.33	8.27

Source: - Security Board Annual Report 2007/08

Banking Sector dominates the whole transaction of Nepal Stock Exchange. 78.12% of the Annual turnover is covered by banking sector only, which indicates that, the investors confidence is basically on banking sector only. Similar is the case with market capitalization and paid up value. Therefore the fate of stock market depends on the performance of banking sector i.e. the whole index of NEPSE is driven by the single sector of Banks.

4.1.7 Some important Trend in Security Market

a. Monetary policy Implication on Security Market

The share market is much unpredictable. Sometimes even decision based on sound financial analysis may go wrong. Because share price are not only based on the expected return of particular company's script but also on overall situation on market, specially demand and supply of shares, investors confidence, brokers behavior and transaction process.

The current share market in Nepal is the verge of collapse. The situation is primarily created due to self-explanatory reason listed in accompanying box.

Macro Reason	Micro Reason
1) Uncertain political atmosphere 2) Institutional inefficiency 3)Directives from NRB	1. Lack of professional advisory institute 2. Broker curtailing 3. Promoter selling shares 4. Lack of Capital market information 5. Non operative market maker

The monetary implication has measure influence in Nepalese share market. The influence of recent directives from NRB can be taken as evidence of our claim. The directive is encouraging as its plan to strengthen commercial bank in the long run. Its objective is to save other commercial banks from becoming Nepal Bank limited and Rastray Banijya Bank Limited. The directive has three-year plan and steps have to be implemented from fiscal year 2058/59 onwards. It has made alteration in the requirements of core capital and supplementary capital but important change form stock markets point of view is loan loss provision instead of six categories previously there are four categories now for loan loss provision. For any loan overdue for more than three month 25 percent of loan amount should be provisioned and this should be 100 percent for loan over one year in arrears. This means, some of the banks may have negative operating profit in first quarter

of the fiscal year 2058/59. This anticipation has led to the decreasing share price of banking institution.

b. Fiscal policy Announcements and Security Market

The announcement of fiscal policy has rendered the major influence on stock market. The introduction of tax dividend at the rate 5% in 2000 A.D. and capital gain tax at the rate of 10% in fiscal year 2001 hindered the bullish tendency in the stock market. Previously both of them were tax-free. However the commission has to be paid to the broker.

If the current market confidence is taken as indicator of the effect of capital gain tax (CGT) certain indication are not encouraging. The week following the budget announcement, the NEPSE index has been falling. The upward movement in stock price till July 16, 2001, followed by continued fall shows the game plan of investors and brokers the tax liability. During the period dummy transfer were made and stock prices pushed up. For example share price of Nepal Bangladesh bank that stood at Rs 937 on July 9 shut up to Rs 1180 by July 16.

The government decision to levy CGT may not be bad, especially in the light of its intention to include all income generating activities under the tax net. And because stock trading is profitable venture this too needs to be taxed. But what about the mechanism and other related aspect. Don't they need proper addressing? This is key question. And this is exactly the case of discontentment of the stock market.

Despite the rationale of charging the CGT from the government's perspective perhaps it was not right at its juncture since only secondary market of the country is on a downturn. In addition when one compares the primary market and secondary market rates, the decision may not have been right. Say, prevailing primary market rates stand at 5% investors makes Rs. 500 over his Rs 1000

investment in stock. In this case the government would charge CGT on Rs 500. But considering the fact that Rs 500 can be obtained from even the bands can this be called the true capital gain? Furthermore, if bank rates were 10% then surely investors would have incurred opportunity capital loss of Rs 500 instead. This is the main reason, which may come as discouraging signal to small investors in stock market.

4.1.8 Factor Affecting the Nepalese Stock Market

As the Nepal stock Exchange is growing in nascent stage, the turnover of stock market capitalization, number of transactions is still very thin. However, the majority of investors in the Nepal stock exchange are individual investors. The volatile and rudimentary mature if Nepalese stock exchange indicates highly dissatisfaction from the investors. It may be mainly due to the lack of awareness amongst the investors, low habit of investing in the stock and holding strategy of the investors. However, most of the individual investors reveled to be isolated and incapable of analyzing the performance of the company in which they have invested. Meanwhile, most of the investors make buy or sell decision without having risk-return analysis and proper evaluation of the company's performance. Nevertheless, the Nepal stock Exchange has been putting lot of efforts in stabilization of the market and its development; it has not been able to achieve the required success in so far. In view of this, this research work has been focused to reveal such qualitative factors, which affects the Nepalese stock market that could be summarized as below.

a. Vulnerable Market Structure

The turnover of the stock in the market is still very thin due to its nascent stage. As such it has not been yet possible to create a continuous market. However, there could be a lot of reason. The majority of the investors in Nepal stock Exchange are individual investors. The volatile and rudimentary nature of Nepalese stock market

indicates highly dissatisfaction from the investors. It may be mainly due to the lack of awareness among the investor's low habit of investing in the stock and holding strategy of investors. However, most of the individual investors are revealed to be isolated and incapable of analyzing the performance of the company in which they have invested. Thus, only the efficient effective way for the majority of stockholders is to follow institutional investors. Therefore, it is convenient for the institutional investors to manipulate the stock price and control the market at the cost of scattered and small investors. Due to such structural lacunas in the Nepalese stock Market, it is very difficult to predict the real market trend. However it has also been revealed that, that in some of the cases, the market response regarding the stock's price round to be quit different from the capital market theory.

b. Structure of the Ownership

In Nepal very few promoters are found to be interested to run a company through huge share participation rather than partnership or sole proprietorship. Though, the company act has some provision for issuance of share capital. To general public most of the companies are revised to be delaying in the issue of shares. Nevertheless, the company issues shares to the general public, the quantum of the issue will proportionately lesser than promoters stake and out of which the relatives of the promoters' stake and out of which the relative of the promoters and the other corporate investors will take large proportion of public issue, most of them would have holding strategy, i.e. they would treat stock purchase as long term investment and wait for handsome dividend or bonus. Thus, this has tremendous impact in stock market for lower level transaction.

c. Economic Factors

The poor state of economy such as, low economic growth, decreasing trade activities, low saving mobilization and widening saving investment gap has

resulted in lower activities in the Nepalese stock market. The ever-increasing saving-investment gap has negative impact in the development of the capital market.

d. Legal Framework

The government policies are always determinant factor to influence the Nepalese stock market. Some of the reason for the low level of activity in the stock market may have to do with tax regulations to mitigate the problems of insider trading and manipulation of market. Thus due to the lack of effective law prohibiting such abuses, and to inactive enforcement of existing laws the stock market is lacking fair game. As an example of the problem, the penalty in current law for insiders who unfairly exploit their position is merely the forfeiture of the shares. However, this is not sufficient deterrent.

e. Lack of Transparent Information

The main factor affecting the stock market is the lack of timely and transparent financial reporting the non-performance of due diligence requirement prior to issuance of new listings. Though, NEPSE is publishing annual report, Trading Report and financial information of listed companies, it has not been so transparent and most of the times those have been found incomplete for public purpose. Thus, the lack of stock market statistics has also influence in squeezing the turnover level as well as slow growth of Nepalese stock market.

f. Market Fundamentals

Many of non-financial listed companies have low profitability and a poor record of distributing dividends. However, most of them were found financially sick. This has also negative impact in the stock market, as the investors want to invest only in the profitable companies. However the banks and financial companies are most attractive amongst investors and also actively traded issues.

g. Lack of strong Monitoring System

Some of the major problems experienced by the stock market are the poor regulatory controls and supervision by securities board and Nepal stock exchange. There are reports that in the case of infractions, when discovered go unpublished. Meanwhile, the problem of insider trading and manipulation of market are also due to lack of strong and effective monitoring system.

One of the influencing factors in lower level of activity is mainly of the exchange. The trading activities are carryout on 'open-out-cry system'. The broker system is yet to be developed; however, the investors themselves of their representatives go directly to the exchange to transact their deals. Moreover, the Nepalese capital market is not yet integrated regionally and globally. Henceforth, all these factors have greater influence in Nepalese stock market. Another serious deficiency in capital market is the complete absence of any provision of law regulating corporate commercial paper and bonds and therefore these financial instruments are not available.

h. Leakage of Secret Information

The Nepalese stock market has also been suffered from several leakage of corporate decision before it has been made public. It is revealed that some of market maker and broker have organizations and get secret information due to their closed intimacy with executives. As a result, the price of stock is manipulated before the secret decision made public. This trend has hindered the Nepalese stock market very deeply. This ahs also evidenced from the several price changes (or manipulation) in the last five years.

4.1.9 Psychology of Nepalese Stock Market

In the short history of Nepalese capital market, it has seen two big crashes. The first crash was in the second half of 1994 and second crash was in the last six

month of 2001. However, it was in bullish trend in initial month of 1994 public sentiments towards the corporate share was so strong that prices of equity shares of most of the companies rises, especially shares of banks and financial companies went up without financial support. When joint venture banks started to declare attractive rates of dividends, investors exhibited grave concern over shares of all companies irrespective of financial strength of companies. The NEPSE index tremendously went up to 265. But this period onwards, the bearish tendency in the market started. Most of the investors were not aware of the security price movement, risk associated with corporate investment. They made a pre-concept of security investment is beneficial that to deposit in banks. The deregulation of interest rate reduced the deposit interest rate of Nepalese market. This flooded the investors to security market. When some Ltd. Act Laboratories started showing poor performance, the investors started to loose their confidence in stock market and rush to sell their shares which result the downturn of the market.

The cause of downturn of stock market in 2001 is little different. The unawareness of investors to corporate investment and the risk associated with it is a common reason. At initial month of years, NEPSE index was showing bullish tendency. It was 548.82 in 23, Nov. 2000, this had been crashed down to 375.17 on March 2001.

The Down turn of stock market started when the NRB directed all the commercial banks to maintain loan loss provision. For any loan overdue for more than three months. 25% of loan amount should be provisioned and this should be 100% for loan over one year in arrears. This means some banks have negative operating profit in first quarter of fiscal year 2058/59. Those who were about to issue bonus share and cash dividend withdrew their decision. This anticipation has lead to the decreasing share price of banking institution. However the uncertain political atmosphere has also major influence in stock price crash.

The frequent market collapse has emphasized the need to correct several deficiencies in out financial system. Financial system comprised of the banks and other depository as well as non-depository financial institution, money markets and capital market. It allows an efficient transfer of resources form the surplus units to deficit unit i.e. form saver to investor. By mobilizing saving to high return investment most effectively an economy can achieve higher return of growth. The development of capital market is closely related to the modernization and development of financial system. The stock market had lost momentum reflecting concern that ore fundamental measure were need to put economy and financial system on path to recovery. The government initiated the policy of economic liberalization in 1985 and first phase measure to reform financial sector was adopted. Joint investment in banking sector was invited, interest rate was deregulated and various provision as to maintenance of capital adequacy ratio, open market operation, exchange market intervention loan loss provision and credit ceiling were made. Now, financial restructuring is broadly on track and the policy for corporate restructuring is largely in place. A strong financial development is underway. All these alone with privatization policy of government have promoted further development of capital market in Nepal.

4.2 Risk and Return of Stock Market

Risk is related to future and future is uncertain. But risk is manageable rather than uncertain. Company-specific risk (earning variability) and company's ability to service its debt burden are intimately related to the particular characteristic of the business or businesses in which the company operates. Moreover, they are affected by economic conditions- apart from management's ability to generate satisfactory operating performance.

There are different types of securities as treasury bills, long-term government bonds, long-term corporate bonds, common stocks etc. among these securities this

study concern with common stocks. “Common stock represents a commitment on the part of a corporation to pay periodically whatever its board of directors deems appropriate as a cash dividend”.

Common-stock holders of a company are its ultimate owners. Collectively they own the company and it is assumed that ultimate risk is associated with ownership. So Common stock is known as risky security. But what is risk? “Risk is like pornography. It’s hard to define, but you know it when you see it. Investors invest in common stock for higher return. But their expected return may or may not change in realities. This uncertainty is a major risk to investors in stock market investment.

The return is income received on an investment, which is expressed as dividend, plus any change in market price of the share (MPS) and usually expressed in percent. Both dividend and market price of the share are uncertain figures. So, the actual return on investment in common stock may differ substantially form the expected return. “The variability of returns from those that are expected is defined as risk. The greater the variability, the riskier the security is said to be. The market price of the share of a company is driven both by fundamental business values and stock market sentiment. For a given business, it is always worth attempting to identify which of these is driving its share price.

Generally, investors are risk averse. They always seek higher return for more risk premium. So the primary problem in investment is to identify the security, which has low risk and high return. Although, return cannot be increased substantially, risk can be reduced by diversification of funds in different stocks making a portfolio. Well diversification can eliminate the unsystematic risk, which is not explained by general market movement. Systematic risk, which is associated with change in return on the market as whole, cannot be avoided by the diversification.

In this study, we are only concerned with common stock return and risk. Return of common stock includes:

1. Income from price appreciation of stock i.e. capital gain or losses.
2. Income form cash dividend and bonds share, which is regularly paid to stockholders every period. Return of different securities can be measured and also compared by holding period yield.

Similarly, like return, risk is another important constituent of investment without considering it is not sensible to talk about return because investment decision involves adequate tradeoff between risk and return. At any time investors may be aware about their wealth position and also concerned with favorable and unfavorable situation, which frequently exists and affects in return. Risk is the actual outcome of unfavorable outcomes. If one forecast already, they could be prepared themselves for that consequences. Investors cannot reasonably expect higher return without assuming risk. If investors want to eliminate risk, they can be insured return in saving accounts. Due to limited and fixed return on deposit once could not earn higher return than that rate. That have opportunity to earn higher return, investors are ready to higher risk. Risk is often associated with variability of return; higher variability means higher fluctuation of return. So, the deviation of the return is measured by dispersion. In an asset return, if there is not variability in effects, there is no risk. Due to uncertain and dynamic mechanism of market, there always exists risk.

4.2.1 Market Capitalization and NEPSE Index

To the analysis of the overall market return, it is essential to identify market capitalization and index of overall market of each sector. Market capitalization is the multiple of market price of share. Market capitalization is the multiple of market price of share and listed number of share of each company in stock exchange.

Table 4.5

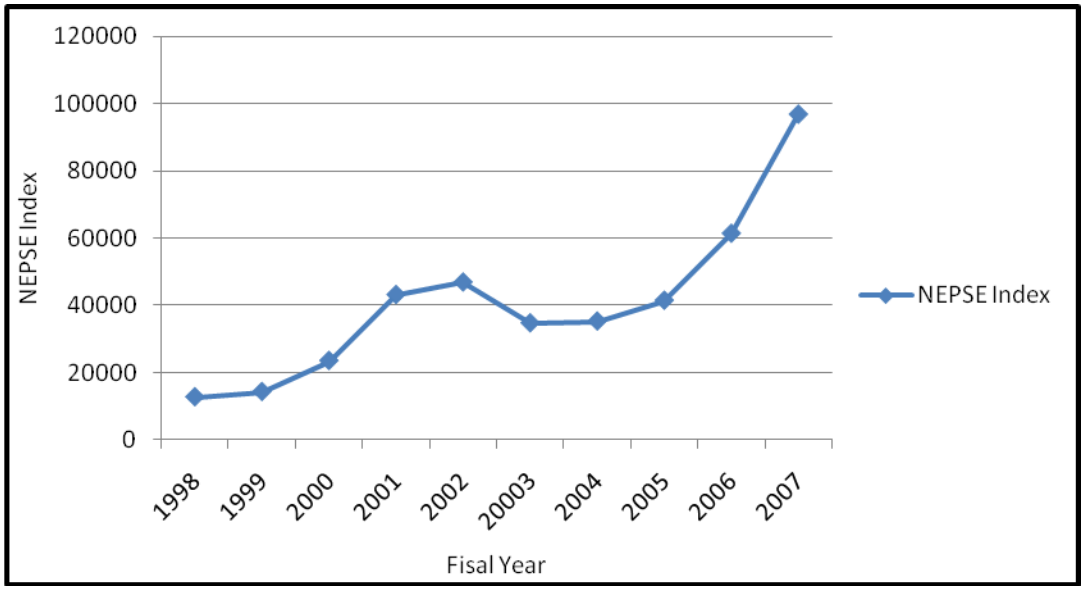
Market Capitalization of Each Sector an Overall Stock Market Capitalization

Year End	1998	1999	2000	2001	2002	20003	2004	2005	2006	2007
Banking	5667.55	6958.97	13632.41	28355.09	31621.71	25861.89	22453.49	27944.27	41169.95	70271.81
Mfg & Processing	2507.84	2611.38	3925.81	5823.00	5971.97	2807.74	4731.30	4644.59	5024.83	5472.11
Hotel	1705.67	1535.93	662.04	660.73	616.98	527.48	488.02	2391.39	2308.38	2344.21
Trading	677.2	654.54	2309.9	3528.55	2969.85	107.12	2550.61	490.37	635.88	764.44
Insurance & Finance	1991.84	2215.83	2557.18	4271.61	5374.69	4328.55	4949.7	5461.05	7632.23	9952.23
Others	147.62	312.36	420.29	484.34	302.89	1071.09	67.26	493.09	4594.62	8008.94
NEPSE Index	12697.7	14269.0	23507.6	43123.3	46858.0	34703.8	35240.3	41424.77	61365.89	96813.74

Source: Security Board, 2006/07

Figure 4.3

Market Capitalization of Each Sector an Overall Stock Market Capitalization



Above table and figure shows the market capitalization of each sectors up-to fiscal year 2006/07. At the beginning, Market capitalization of all the sectors were higher. Since fiscal year 1997/98 Market capitalization was in increasing stage up to year fiscal year 2001/02. Then again it was decreasing up to fiscal year 2003/04. After fiscal year 2003/04 it is again in increasing stage. In Comparison to the sect oral return, Market capitalization of Banking Insurance and Financial companies

are higher than other sectors. So it can be seen the whole market is dominated by Banking, Insurance and financial sectors.

Table 4.6

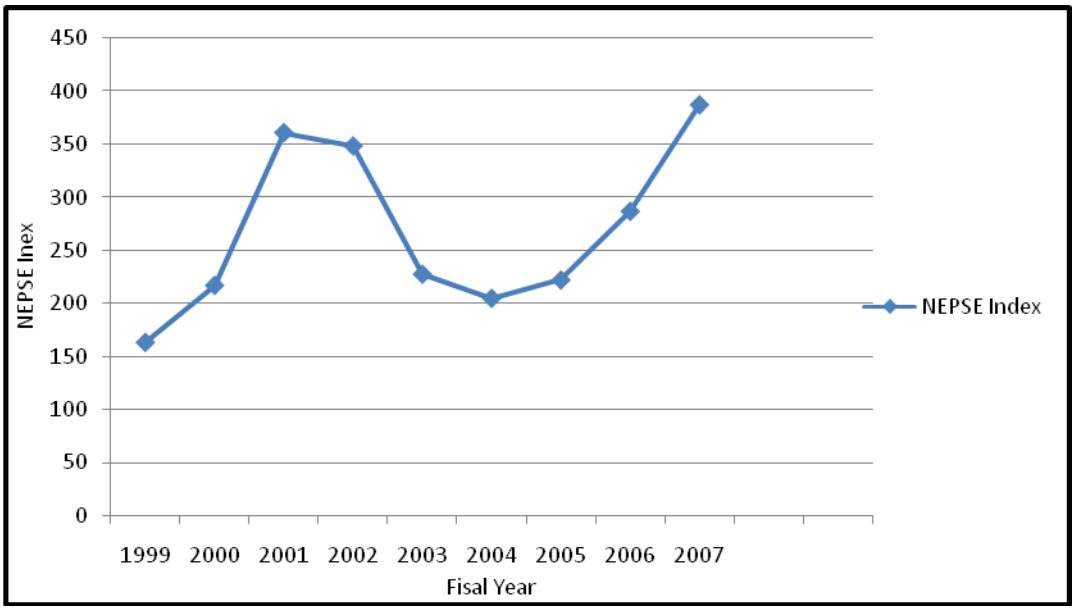
Sector Wise Year-end Index up to 2007

Sector	1994	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Banking	100	167.20	150	219.04	397.17	384.08	241.15	223.31	211	271.25	365.945
Manu & process	100	168.53	162.79	229.83	340.59	349.31	273.67	250.13	255.58	276.5	301.11
Hotel	100	277.46	249.85	242.52	346.15	291.34	216.51	196.68	184.41	178	180.77
Trading	100	156.69	122.58	123.99	123.74	115.55	102.2	94.56	95.01	123.2	148.11
Insurance & Finance	100	164.19	175.56	195.68	305.98	325.89	288.75	224.64	216.805	274.315	321.31
Others	100	228.27	279.51	376.10	308.46	192.9	77.34	48.56	142.65	347.65	410.00
NEPSE Index	100	176.31	163.35	216.93	360.70	348.25	227.54	204.86	222.04	286.67	386.83

Source: Security Board, 2006/07

Figure 4.4

Sector Wise Year-end Index up to 2007



Similarly, above table and figure shows, represents year-end (min-July) index of each year up to 2006/2007 after establishment of NEPSE. Overall market index was decreasing up to 1998. After the fiscal year 1998/99, the situation was improving up to fiscal year 2006/07. It is remained unsatisfactory due to the poor economic condition still existing in the country. Out of them Hotels sector was in decreasing stage. According to daily transaction, banking sectors leads in the secondary market. That is way overall index is dominated by banking sectors rather than manufacturing and other sectors.

Table 4.7

Computation of Overall Market Return

Year End	NEPSE Index	$R_m = \frac{MI_t - MI_{t-1}}{MI_{t-1}}$	$R - \bar{R}$	$\left(R - \bar{R}\right)^2$
1995 Feb 13	100			
1998	176.31			
1999	163.35	-0.07350689	-0.189583501	0.035941903
2000	216.93	0.328007346	0.211930735	0.044914636
2001	360.70	0.662748352	0.546671741	0.298849992
2002	348.25	-0.03451622	-0.150592831	0.0226782
2003	225.54	-0.34661881	-0.462695421	0.214087052
2004	204.86	-0.09967478	-0.215751391	0.046548662
2005	222.04	0.083862149	-0.032214462	0.001037771
2006	286.67	0.29107368	0.174997069	0.030623974
2007	386.83	0.34931286	0.233314675	0.054435737
Total		0.1160766113		0.0749117927

Source: Security Board, 2006/07

Market return implies that overall return on stock market. It may be based on index of stock Market

According to formula:

$$\left[R_m = \frac{MI_t - MI_{t-1}}{MI_{t-1}} \right] \times 100$$

Where,

R = Average rate of return

MI_t = Index of Period 't'

MI_{t-1} = Index of period't-1'

$$\overline{R_m} = \frac{\sum R}{N} = \frac{1.160766113}{10} = 0.116076611$$

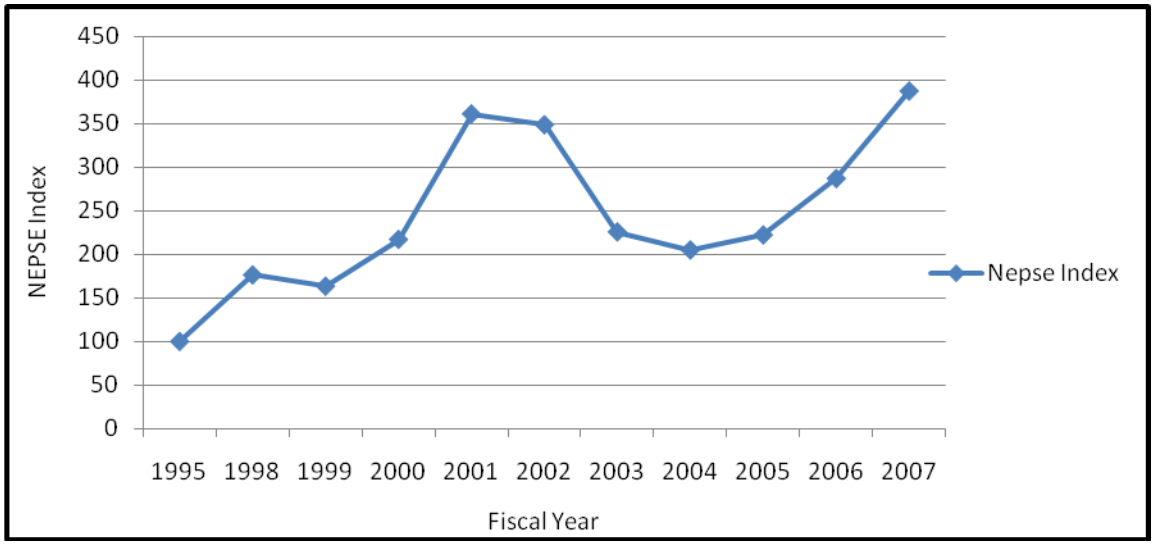
$$\sigma^2 = \frac{1}{N} \times \sum (R - R)^2 = \frac{1}{10} \times 0.749117927 = 0.074911792$$

$$\sigma = \sqrt{\sigma^2} = \sqrt{0.074911792} = 0.273700187$$

$$C.V. = \frac{\sigma}{\overline{R_m}} = \frac{0.273700187}{0.116076611} = 2.357927107$$

Figure 4.5

Computation of Overall Market Return



4.2.2 Risk and Return of Banking Sectors

a) Sectoral Return

Most of the commercial Banks are established under the company Act 1964 with an objective of the bank is to provide modern banking facilities like tele banking to the business, industrialists and other professionals and to provide loans on agriculture, commerce and industrial sectors. Most of the Banking companies are

established and listed in stock exchange limited. These companies are largely traded in secondary market rather than other companies. These sectors represent 78.12% of total transaction in stock market.

Table 4.8

Computation of Risk and Return of Banking Sector

Year End	Nepse Index	$R_B = \frac{BI_t - BI_{t-1}}{BI_{t-1}}$	$\left(R - \overline{R_B}\right)$	$\left(R - \overline{R_B}\right)^2$
1995 Feb 13	100			
1998	167.20			
1999	150	-0.10287081	-0.137394993	0.018877384
2000	219.04	0.460266667	0.33158755	0.110994756
2001	397.17	0.81323046	0.686122548	0.47076415
2002	384.08	-0.03295818	-0.16006092	0.025621153
2003	241.15	-0.37213601	-0.499243922	0.249244493
2004	223.31	-0.07397885	-0.201086762	0.040435885
2005	211	-0.055125162	-0.182233074	0.033208893
2006	271.25	0.285545023	0.158437111	0.025102318
2007	365.945	0.34910599	0.221998078	0.049283146
Total		0.1271079129		0.1023532179

$$\overline{R_B} = \frac{\sum R}{N} = \frac{1.271079129}{10} = 0.127107912$$

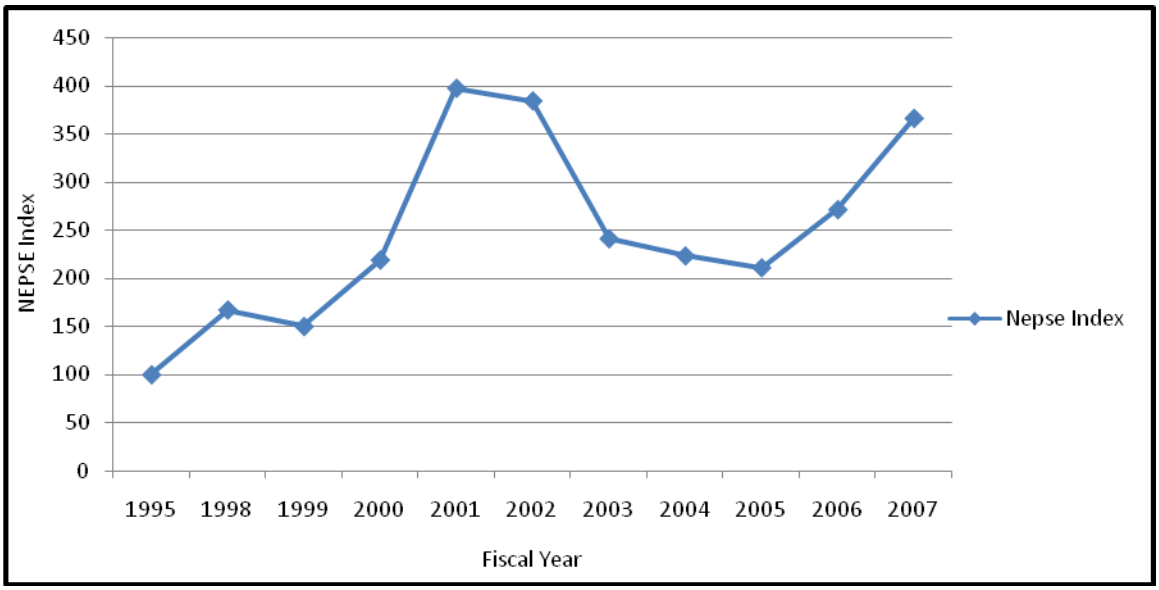
$$\sigma^2 = \frac{1}{N} \times \sum (R - R)^2 = \frac{1}{10} \times 1.023532179 = 0.102353217$$

$$\sigma = \sqrt{\sigma^2} = \sqrt{0.102353217} = 0.319926894$$

$$C.V. = \frac{\sigma}{R} = \frac{0.319926894}{0.127107912} = 2.516970734$$

Figure 4.6

NEPSE Index of Banking Sector



Market return of Banking Sector has around to overall Market return i.e. 12.71%. Similarly, standard deviation and coefficient of variation are 31.99% and 251.69% respectively. Right from fiscal year 2001/02, return of banking sector was in decreasing stage due to the worse economic condition of the country but year after 2004/05 it was going up.

The hypothesis would be tested to find whether the returns from banking companies are equal or not, by using the different mean of t-statistic.

The hypothesis would be

H_0 : There is no significance difference between overall market return and return of banking sectors. i.e. return of banking sector is equal to overall market return.

H_1 : There is a significant difference between overall market return and return of banking sector i.e. return of banking sector is not equal to overall market return.

i.e. t = statistic under H0 is: $= \frac{\overline{R_B} - \overline{R_m}}{\sqrt{s^2}\left(\frac{1}{n1} + \frac{1}{n2}\right)} \approx t_{n1+n2} - 2$

By applying the formula under null hypothesis the calculated value is equal to $|t| = 0.0786$

In 18 degree of freedom. The tabulated values in different level of alpha (α) are:-

$t_{0.01} = 2.878$
$t_{0.05} = 2.101$
$t_{0.10} = 1.734$

(Since almost business research has based on 5% level of significance)

Since the calculated value of 't' is less than the tabulated value of 't', it is not significant, so null hypothesis may be accepted in 5% level of significant and we conclude that sample return from normal population with same return i.e. there is no significant difference between sample return and market return. The hypothesis also proved that securing return of banking sector as compared to market return has equally benefited people.

b) Return of Individual Companies

The calculation of stock return includes the income from capital appreciation each stock, cash dividend and bonus share in every period. This study would follow holding period return to calculated return of each company. Standard deviation, variance and coefficient of variation are also calculated to analyze risk and return associated stocks. Regarding this, by suing the t-statistic of single mean

individually, it helps to find out whether the return of individual companies are different from overall market return or not.

The hypothesis would be:

H_0 : There is no significance difference between overall market return and return of banking sectors. i.e. return of Banking sector is equal to overall market return.

H_1 : There is a significant difference between overall market return and return of banking sector i.e. return of banking sector is not equal to overall market return.

i.e. t = statistic under H0 is:

$$= \frac{\overline{R_B} - \mu}{\frac{S}{\sqrt{n}}} \approx t_{n-1}$$

i) Standard Chartered Bank Limited

Standard Chartered Bank limited (Former Grindlays Bank limited) was established under the company act 1964 in 1985 as a second foreign joint-venture bank. Average market return, standard deviation and coefficient of variation from 1997/98 to 2006/07 were 42.09%, 42.97% and 101.97% respectively. Due to high cash dividend as well as Bonus share, high market price of share, return was increased up to 82.63% at the end of year 2006/07.

To test the hypothesis between overall market return and return of this company, to find out average return of this company is equal or not to market return, the t-statistic of sample mean test has been employed for this purpose. Since the calculated value 't' is equal to 2.0624, the null hypothesis has been accepted at 5%

level of significance for two tailed in 8 degrees of freedom i.e. return of this company does not signify difference between overall market return.

ii) Bank of Katmandu

The Bank was established in 1993 in collaboration with the SIAM Commercial Bank PCC, Thailand under the company Act, 1997. Average Market return, Standard deviation and Coefficient of Variation from 1997/98 to 2006/07 were 82.85%, 124.52% and 150.29% respectively. Due to good cash dividend, Bonus share and high market price of share, return was increased up to 344.36% in the end of 2000 and second highest was 125.58% in the end of 2005/06.

To test the hypothesis between overall market return and return of this company, to find out average return of this company is equal to not to market return, the t-statistic of sample mean test has been employed for this purpose. Since the calculated value 't' is equal to = 1.5137, the null hypothesis has been accepted at 5% level of significance for two tailed in 7 degree of freedom i.e. return of this company does not signify difference between overall market return.

iii) Himalayan Bank Limited

Himalayan Bank limited is a joint-venture bank with Habib Bank Limited of Pakistan, was established in 1992 under the company Act, 1964. This is the first joint-venture bank managed by Nepali Chief Executive. The operation of the bank started from 1993 February. Average Market return, Standard deviation and Coefficient of Variation from 1997/98 to 2006/07 were 47.03%, 50.19% and 106.72% respectively. Due to good cash dividend, Bonus share and high market price of share, return was increased up to 95.364% at the end of 1999.

To test the hypothesis between overall market return and return of this company, to find out average return of this company is equal or not market return, the t-statistic of sample mean test has been employed for this purpose. Since the calculated value 't' is equal to 1.9960 the null hypothesis has been accepted at 5% level of significance for two tailed in 8 degree of freedom i.e. return of this company does not signify difference between overall market return.

iv) Nabil Bank Limited

Nepal Arab Bank Limited, the first joint-venture commercial bank, was incorporated in 1984. Dubai Bank ltd. was the initial foreign joint-venture partner with 50 percent equity investment. The shares owned by Dubai Bank limited, (DBL) were transferred to Emirates Bank international Limited, Dubai by virtue of its annexation with the later. Latter on, emirates Bank International Limited, Dubai sold its entire 50 percent equity holding to national bank ltd., Bangladesh. National Bank ltd., Bangladesh is managing the bank in accordance with the Technical services Agreement signed between it (NBL) and the bank on June 1995.

Average Market return, Standard deviation and Coefficient of Variation from 1997/98 to 2006/07 were 39.58%, 41.80% and 105.62% respectively. Due to Low stock dividend, return was decreased up to 49% at the end of 2003.

To test the hypothesis between overall market return and return of this company, to find out average return of this company is equal or not market return, the t-statistic of sample mean test has been employed for this purpose. Since the calculated value 't' is equal to 1.892 the null hypothesis has been accepted at 5% level of significance for two tailed in 8 degree of freedom i.e. return of this company does not signify difference between overall market return.

v) Nepal SBI Bank Limited

Nepal SBI Bank Ltd. was registered under the company Act, 1964 in 1993. This is the joint-venture of State Bank of India and Nepali promoters. The bank is managed by state Bank of India under the joint-venture and technical services agreement signed between it and Nepali promoters Viz. Employees Provident Fund and Agriculture Development Bank, Nepal. The state Bank of India is holding its 50 percent equity.

Average market return, Standard deviation and Coefficient of Variation from 1997/98 to 2006/07 were 18.47% to 52.25% and 282% respectively. Due to good cash dividend, Bonus share and high market price of share, return was increased up to 35.639% at the end of 2002.

To test the hypothesis between overall market return and return of this company, to find out average return of this company is equal or not to market return, the t-statistic of sample mean test has been employed for this purpose. Since the calculated value 't' is equal to 0.3716, the null hypothesis has been accepted at 5% level of significance for two tailed in 8 degree of freedom i.e. return of this company does not signify difference between overall market return.

vi) Nepal Bangladesh Bank Limited

Nepal Bangladesh Bank Limited, a joint venture bank with I.F.I.C. Bank Ltd. Of Bangladesh, was established in 1993 under the company Act, 1964. Average market return, Standard deviation and coefficient of Variation from 1997/98 to 2006/07 were 64.73%, 123.41% and 190.64% respectively. Due to good cash dividend, Bonus share and high market price of share, return was increased up to 322.40% at the end of 2001.

To test the hypothesis between overall market return and return of this company, to find out average return of this company is equal or not to market return, the t-statistic of sample mean test has been employed for this purpose. Since the calculated value 't' is equal to 1.0544, the null hypothesis has been accepted at 5% level of significance for two tailed in 6 degree of freedom i.e. return of this company does not signify difference between overall market return.

vii) Everest Bank Limited

Everest Bank Ltd. was established in 1992 under the Company Act, 1964 with an objective of carrying out commercial banking activities under the Commercial Bank Act, 1974. Average Market return, Standard deviation and Coefficient of Variation form 1996/97 to 2005/06 were 54.76%, 63.78% and 116.45% respectively. Due to good cash dividend, Bonus share and high market price of share, return was increased up to 61.37% at the end of 2006/07.

To test the hypothesis between overall market return and return of this company, to find out average return of this company is equal or not to market return, the t-statistic of sample mean test has been employed for this purpose. Since the calculated value 't' is equal to 1.9140, the null hypothesis has been accepted at 5% level of significance for two tailed in 8 degree of freedom i.e. return of this company does not dignify difference between overall market return.

In summary we can also present in table.

Table 4.9

Summary Tables of the Sample Companies

SN	Companies	$\lvert t\rvert = \frac{\overline{R_B} - \mu}{\frac{s}{\sqrt{n}}} \approx t_{n-1}$	D.F.	Tabulated Value (at 5% level of Significance)	Accepted and rejected in each level of significance
1.	Standard Chartered Bank Limited	2.062431621	8	2.306	H0 accepted
2.	Bank of Kathmandu	1.513776586	7	2.365	”
3.	Himalayan Bank Ltd.	1.996036506	8	2.306	”
4.	Nabil Bank Ltd	1.892575558	8	203.6	”
5.	Nepal SBI Bank Ltd.	0.371671613	8	2.306	”
6.	Nepal Bangladesh Bank Ltd.	1.054456831	8	2.306	”
7.	Everest Bank Ltd.	1.914004634	8	2.306	”

4.2.3 Risk and Return of Insurance and Finance Companies

a) Sectoral Return

Most of the finance and Insurance companies were established and listed in stock exchange limited after liberalization policy was accepted. These companies are frequently trend in secondary market rather than other sectors (except banking sectors). The main objectives of the insurance companies are to providing non-life insurance services in the field of fire, marine, vehicle and miscellaneous insurance in the country and abroad. These companies have obtained permission to commence insurance business from insurance board under insurance Act 1992. Similarly, most of the finance companies were established under the company Act 1964 with an objective of the Company is to collect deposits, to provide short-term and long-term loans and other financial services under Finance Company Act, 1985. Recently, 64 insurance and finance companies have been listed and frequently traded in stock exchange representing 12.62% of the total transaction in stock market.

Table 4.10

Computation of Fisk & Return of Insurance & Finance Sector

Year End	NEPSE Index	$R_{IF} = \frac{IFI_t - IFI_{t-1}}{IFI_{t-1}}$	$\left(R - \overline{R_{IF}}\right)$	$\left(R - \overline{R_{IF}}\right)^2$
1994 Feb 13	100			
1998	164.19			
1999	175.56	0.069249041	-0.018581855	0.00345285
2000	195.68	0.114604694	0.026773798	0.000716836
2001	305.98	0.563675388	0.475844492	0.22642798
2002	325.89	0.065069612	-0.022761284	0.00518076
2003	288.75	-0.11396483	-0.201795726	0.040721515
2004	224.64	-0.22202597	-0.309909059	0.096043625
2005	216.805	-0.034878027	-0.122708923	0.015057479
2006	274.315	0.26526141	0.177430514	0.031481587
2007	321.31	0.171317645	0.083486749	0.006970037
Total		0.0878308963		0.0227490101

$$\overline{R_{IF}} = \frac{\sum R}{N} = \frac{0.878308963}{10} = 0.087830896$$

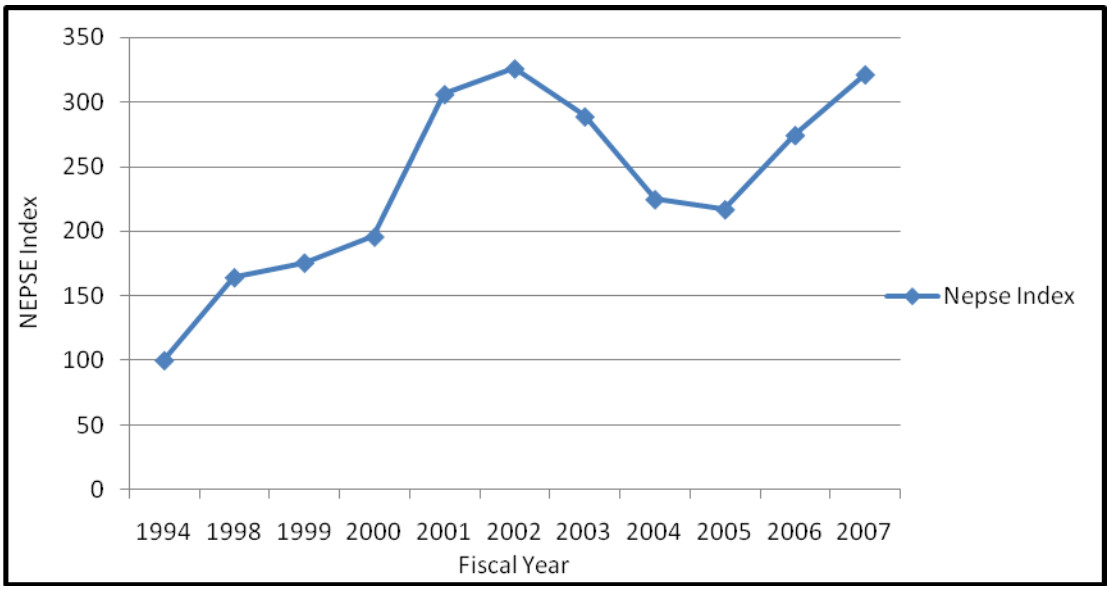
$$\sigma^2 = \frac{1}{N} \times \sum (R - R)^2 = \frac{1}{10} \times 0.227490101 = 0.02274901$$

$$\sigma = \sqrt{\sigma^2} = \sqrt{0.02274901} = 0.15827749$$

$$C.V. = \frac{\sigma}{R} = \frac{0.150827749}{0.87830896} = 1.717251635$$

Figure 4.7

NEPASE Index of Insurance and Finance Companies



Market return of Insurance and Finance sector have around to overall market return i.e. 8.78%. Similarly standard deviation and Coefficient of variation are 15.08% and 171.72% respectively. In previous year, return of insurance and finance sector was in decreasing stage. Now existing situation was improving and condition of insurance of finance sector was improving through after fiscal year 2004/05.

The hypothesis would be tested to find whether the return from insurance and finance companies are equal or not, by using the different mean of t-statistic.

The hypothesis would be:

H_0 : There is no significance difference between overall market return and return of Insurance and Finance companies i.e. return of Insurance and Finance companies is equal to overall market return.

H_1 : There is a significant difference between overall market return and return of Insurance and Finance companies i.e. return of Insurance and Finance companies is not equal to overall market return.

T-statistic under H0 is:

$$= \frac{\overline{R_{IF}} - Rm}{\sqrt{S^2\left(\frac{1}{n1} + \frac{1}{n2}\right)}}$$

$$= \frac{0.08783 - 0.11607}{\sqrt{0.054256\left(\frac{1}{10} + \frac{1}{10}\right)}}$$

$$= \frac{-0.02824}{0.23294}$$

$$= \text{-0.857}$$

By applying the formula under null hypothesis the calculated value is equal to $|t|$ = 0.857 in 18 degree of freedom. The tabulated values in different level of alpha (α) are:

$t_{0.01} = 2.878$
$t_{0.05} = 2.101$
$t_{0.10} = 1.734$

(Since almost business research has based on 5% level of significance)

Since the calculated 't' is less than the tabulated 't'. it is not significant, so, null hypothesis may be accepted in 5% level of significant and we conclude that sample return form normal population with same return i.e. there is not significant difference between sample return and market return. The hypothesis also proved that securing return of insurance and finance companies as compared to market return has equally benefited people.

b) Return of Individual Companies

The calculation of stock return includes the income from capital appreciation each stock, cash dividend and bonus share in every period. This study would follow holding period return to calculated return of each company. Standard deviation, variance and coefficient of variation are also calculated to analyze risk and return associated stocks. Regarding this, by suing the t-statistic of single mean individually, it helps to find out whether the return of individual companies are different from overall market return or not.

The hypothesis would be:

H_0 : There is no significance difference between overall market return and return of Insurance and Finance Companies i.e. return of Insurance and Finance Companies is equal to overall market return.

H_1 : There is a significant difference between overall market return and return of Insurance and Finance Companies i.e. return of Insurance and Finance Companies is not equal to overall market return.

i.e. t=statistic under H0 is:

$$= \frac{\overline{R_{IF}} - \mu}{\frac{S}{\sqrt{n}}} \approx t_{n-1}$$

i) Kathmandu Finance Limited

Kathmandu Finance Limited was established under the Company Act, 1964 in 1994. Average Market. Standard deviation and Coefficient of Variation from 1997/98 to 2006/07 were 40.38%, 71.83% and 177.88% respectively. The highest return of this company was 217.34% in 2001 due to high fluctuation of share price. The company declared 50% and 9.473% stock dividend only in F/Y 2003/04 and 2005/06. The market price of this company in these days is in increasing stage.

To test the hypothesis between overall market return and return of this company, to find out average return of this company is equal or not to market return, the t-statistic of sample mean test has been employed for this purpose. Since the calculated value 't' is equal to 1.1330, the null hypothesis has been accepted at 5% level of significance for two tailed in 8 degree of freedom i.e. return of this company does not signify difference between overall market return.

ii) Annapurna Finance Company Limited

Annapurna Finance Company Limited was established on 1993 under the Company Act, 1964. This is the first company established outside Kathmandu valley. Average Market return, Standard deviation and Coefficient of Variation from 1997/98 to 2006/07 were 32.06%, 49.16% and 153.28% respectively. The highest return of this company was 155.56% in 2001 due to high fluctuation of share price. The company declared 50%, 59.9% and 10% stock dividend in F/Y 2004/05, 2005/06 and 2006/07 respectively. The market price of this company in these days is in satisfactory stage.

To test the hypothesis between overall market return and return of this company, to find out average return of this company is equal or not to market return, the t-statistic of sample mean test has been employed for this purpose. Since the calculated value 't' is equal to 1.1772, the null hypothesis has been accepted at 5% level of significance for two tailed in 8 degree of freedom i.e. return of this company does not signify difference between overall market return.

iii) Premier Insurance Company (Nepal) Limited

Premier Insurance company (Nepal) Limited was established under the company Act, 1964 in 1992. Average Market return, Standard deviation and Coefficient of Variation from 1997/98 to 2006/07 were 12.68%, 37.56% and 296.164%

respectively. The highest return of this company was 108% in 2001 due to high fluctuation of share price. The company has been increasing right form 2004/05.

To test the hypothesis between overall market return and return of this company, to find out average return of this company is equal or not to market return, the t-statistical of sample mean test has been employed for this purpose. Since the calculated value 't' is equal to 0.0809, the null hypothesis has been accepted at 5% level of significance for two tailed in 8 degree of freedom i.e. return of this company does not signify difference between overall market return.

iv) United Insurance Company Limited

United Insurance Company Limited was established in 1992 with an objective of providing non-life insurance services in the field of fire, marine, vehicle and miscellaneous insurance in the country and abroad. Average Market return, Standard deviation and Coefficient of Variation from 1997/98 to 2006/07 were 11.95%, 36.12% and 302.10% respectively. The highest return of this company was 92.91% in 2001 due to high fluctuation of share price. The company has not been declared stock dividend yet. The market price of this company has been decreasing but is ha shown some expectation from 2004/05.

To test the hypothesis between overall market return and return of this company, to find out average return of this company is equal or not to market return, the t-statistic of sample mean test has been employed for this purpose. Since the calculated value't' is equal to 0.0255, the null hypothesis has been accepted at 5% level of significance for two tailed in 7 degree of freedom i.e. return of this company does not signify difference between overall market return.

Table 4.11

Summary Table of the Sample Companies of Finance and Insurance Sector

SN	Companies	$\lvert t\rvert = \frac{\overline{R_{IF}} - \mu}{\frac{s}{\sqrt{n}}} \approx t_{n-1}$	D.F.	Tabulated Value (At 5% level of significance)	Accepted and rejected in each level of significance
1.	Kathmandu Finance Ltd.	1.133013795	8	2.306	Ho accepted
2.	Annapurna finance Co. Ltd.	1.177285246	8	2.306	”
3.	Premier Insurance Co. Ltd.	0.080984625	8	2.306	”
4.	United Insurance Co. ltd	0.025593027	7	2.365	”

4.2.4 Market Value of Banking, Insurance and Finance Companies

Market capitalization means the value of firm. Generally, Market capitalization is equals to the number of share outstanding multiplied by shares prices. If other things are constraints, large market capitalization means smaller stock return, higher liquidity and marketability whereas smaller stock provides higher stock return and less utility than longer market capitalization.

Market capitalization may have the function of divided per share, earning per share, return on equity, price earning etc. as constraint with risk and return, it also functions of liquidity leverage, earning and coverage. In the study of Dividend per share, return equity and dividend yield have significant impact but return on equity and price earnings has not fond significant impact in market price of top ten companies, which are trade in Nepal Stock Exchange Limited in fiscal year 1996/97.

To analyze the value of firm (Market capitalization and determinant factors of market value of firm of each sector (i.e. insurance, Finance and Banking sectors), this study includes 7 banking companies 4 Finance and Insurance companies. The

sample is based on market capitalizations, which are frequently traded in stock market. Up to 9 year's data of related companies are included for analytical purpose.

1. Banking Companies

a) Standard Chartered Bank Limited
b) Bank of Kathmandu
c) Himalayan Bank Limited
d) Nabil Bank Limited
e) Nepal SBI Bank Limited
f) Nepal Bangladesh Bank Limited
g) Everest Bank Limited

2. Insurance and Finance Companies

a) Kathmandu Finance Limited
b) Annapurna Finance Company Limited
c) Premier Insurance Company Limited
d) United Insurance Company Limited

The model of multiple regressions is employed to test and analyze the relationship between dependent and independent variables. This model also helps to analyze critically to find cause and effects of dependent and independent variables. The model of multiple of multiple regression equation could be expressed by:

$$Y = f\ (X1, X2, X3, X4, X5, X6)$$

Where,

Y = Market value of firm i.e. market capitalization.

X1 = Earning per share i.e. earning after tax divided by number or share Outstanding.

X2 = Dividend per share i.e. equity dividend divided by number or share outstanding

X3 = Price earning ratio i.e. closing market price of stock divided by earning per share.

X4 = Earning yield i.e. earning per share divided by closing market price.

X5 = Dividend yield i.e. dividend per share divided by closing price of share.

X6 = Return on equity i.e. earning per share divided by paid up price multiplied by 100

Assumptions

Since the market capitalization represent the market value of the firm the market capitalization (in million) data are assumed as dependent variable for the study. Market capitalization is basically dependent on DPS, EPS, EY and ROE data relating to the sample companies are assumed as independent variable. According to the relationship between dependent and independent factors, EPS, EY and ROE have a positive impact in Market capitalization. The higher dividend reduced retain earning as well as market value of firm due to low capital formation in companies. Thus DPS and DY have negative impact in Market capitalization.

4.3 Time Series Data of Sample Companies

4.3.1 Time Series Data of Commercial Banks

"Time series may be defined as collection of readings belonging to different time periods of some economic variable or composite variables". (Gupta, 1996:754) these technique can also be applied, for the study of the behavior of any

phenomenon chronologically over a period in any discipline relating to different studies.

This series data of each year may be constructed by averaging the total sum of each company of specific time period. Table 4.12 shows that time series data of each period of sample companies.

Table 4.12

Time Series Data of Sample Companies of Commercial Bank form 1998-2007

Year	y (Mkt Capt)	X1 EPS	X2 DPS	X3 P/E	X4 D/Y	X5 E/Y	X6 ROE
1998	746.981	55.882	33.502	4.196	5.228	10.11	55.882
1999	752.731	57.1	37.156	4.44	6.548	11.048	57.1
2000	1372.964	55.832	32.565	16.061	4.231	7.905	55.832
2001	3093.65	74.041	36.107	19.014	2.551	5.664	74.041
2002	3939.434	61.624	24.648	42.595	1.374	4.54	61.624
2003	2415.664	45.652	23.285	26.103	2.164	5.292	45.652
2004	2464.25	30.51	32.386	14.721	3.96	7.44	30.51
2005	3105.165	32.814	34.167	80.825	4.78	6.31	32.814
2006	4019.81	41.835	43.316	17.565	3.62	5.91	41.835
2007	6883.63	52.195	48.83	24.94	2.44	4.47	52.195

Earning per share, dividend per share, dividend yield were in increasing and decreasing stage in corresponding fiscal years. Price earning ratio is in increasing stage. Earning yield and return on equity increased less than above factor. Market capitalization was in decreasing stage. In the fiscal year 2000/2001, market capitalization was higher than late and early year.

a) Multiple Correlation Analysis

The multiple correlation of the above table has been done to analyze the relationship of these depended and independent variables. According to their relationship the higher co-related factors (i.e. positive or negative) are selected for multiple regression analysis.

The multiple correlation of the time series data's are:

Table 4.13
Multiple Correlations of Commercial Banks

		MC	EPS	DPS	PE	DY	EY	ROE
Column1	MC	1.000						
Column2	EPS	.278	1.000					
Column3	DPS	-.573	.123	1.000				
Column4	PE	.759	.035	-.784	1.000			
Column5	DY	-.766	-.274	.814	-.885	1.000		
Column6	EY	-.867	-.392	.740	-.775	.914	1.000	
Column7	ROE	.245	.996	.163	.003	-.230	-.363	1.000

According to the above table Market Capitalization has higher negative correlation with Dividend per share, Dividend yield and earning yield. Earning per share has a positive relationship with Dividend per share, Price earning and Return on equity. Dividend per share has also a positive relationship with dividend yield, earning yield and return on equity. Similarly, price earning multiple has a positive relationship with Return on equity. And Dividend yield has a positive relationship with earning yield.

According to the higher relationship, employing elimination process chooses only five variables. That is why, earning per share, dividend per share, dividend yield, earning yield and Return on equity is selected for multiple regression analysis.

In summary output is found by employing 5 variables in the multiple regression analysis of 9-year time series data are.

Multiple R	.912
R Square	.832
Adjusted R square	.551
Standard error	793.13
DW	2.377

Observations 9

Multiple R is equal to 91.2%. Adjusted R square of 9 observations is equal to 55.1%. It states that market capitalization is caused to change 55.1% by those independent variables. Rests of the other variables have less impact on market capitalization i.e. 44.9%. R-square implies the percentage of relationship between these variables in 9 observations. R square is found out to be 83.2%. Similarly Standard error indicates the size of the error in sampling that has been made and also has accuracy of sample that has been estimated to use sample statistic to estimate the larger standard error. The population of the standard error of above nine observations is equal to 793.13.

Table 4.14

Coefficient and P-value of Five Variables

Predicators	Coefficient	Standard error	t-stat	p-value
Intercept	5204.521	2615.212	1.990	0.141
Variable X1	265.777	372.938	.713	0.527
Variable X2	103.090	116.402	.886	0.441
Variable X3	119.802	451.548	.265	0.808
Variable X4	-687.260	335.042	-2.051	0.133
Variable X5	-296.310	371.985	-.797	0.484

(X1=EPS; X1= DPS; X3=DY; X4=EY; X5=ROE)

Dependent Variable: MC

The regression equation of Five Variables is found to be:

$Y=5204.521+266.77X_1+103.09X_2+119.80X_3-687.26X_4-687.26X_5$

(.141) (.527) (.441) (.808) (0.133) (.484)

b)Test of Hypothesis

Above table states that the ‘t’ value of Earning per share came to be .713. Since the calculated t-value is less than the tabulated value at 5% level of significance at 8 degree of freedom. The null hypothesis of Market capitalization is dependent of

EPS is accepted. It states that there is significant positive relationship between market capitalization and EPS. The co-efficient value of X1 indicated that EPS has significant positive impact in Market capitalization.

The DPS also found to be positively related to market capitalization. The positive co-efficient value of DPS and the t-value are respectively 103.090 and 0.886. Since calculated t-value is less that the tabulated value at 5% level of significance at 8 degree of freedom. Null hypothesis of Market capitalization is dependent to DPS is accepted. It also stated that there is a significant positive relationship between market capitalization and DPS of Commercial Banks of Nepal

The Dividend yield and Market Capitalization came to be significant positive relationship. The calculated t-value is .265 and the coefficient value is 119.802. It states that the percent increase in each variable is caused to increase the given amount in market capitalization.

Similarly, the negative co-efficient by -687.260 and calculated t-value -2.051 states that there is significant negative relationship been the value of firm and earning yield. The null hypothesis of market capitalization is independent of EY is rejected in 5% level of significant. It states that the percentage decrease in each variable is caused to increase the given amount of Market Capitalization.

Likewise, t-static and co-efficient value of ROE are negative that -.797 & -296.310 respectively. The alternative hypothesis of Market Capitalization is accepted. It implies that ROE has negative significant impact in Market Capitalization. The percentage decrease in ROE has positive impact in market capitalization.

The analysis shows that EPS, DPS, DY, EY and ROE are significant determinants of Market Capitalization. The Multiple co-efficient of correlation states that the relationship between Market capitalization as dependent variable and all independent variable are highly significant and 91% of the variation in Market Capitalization is explained by the independent variables i.e. EPS, DPS, EPS,EY & ROE.

4.3.2 Time Series Data of Insurance and Finance Companies

To meet overall objective of economic development banking, financial institution, trading and manufacturing industries contribute pivotal role in nation. Prosperity of these areas is the indication of overall economic development. The role of Insurance and Finance Companies cannot be minimized as a main part of economic activities.

The higher market capitalization is profound idea to measure the success of companies. It is the cause of increasing market index and stock return. These two variables are powerful predictors of average stock return. That is why; the study is not enough without analyzing quantitative variables, which have significant impact in market capitalization i.e. market value of firm. If we consider the risk and return, market capitalization may be function of DPS, EPS, P/E and ROE, DY and EY etc. As constrain with risk and return it is also function of liquidity, leverage Earnings, Coverage etc. To analyze the value8e of firm of Insurance and Finance Companies form risk and return site, the time series data of 9 years are employed for this purpose. The following table 4.15 shows that the time series data of each period of sample companies.

Table 4.15

Time Series Data of Insurance and Finance Companies

Year	Y	X1	X2	X3	X4	X5	X6
	(Mkt Capt.)	(EPS)	(DPS)	(P/E)	D/Y)	(E/Y)	(ROE)
1998	27.92	23.082	6.042	7.945	6.632	18.385	23.082
1999	29.742	36.702	8	4.69	7.707	29.457	35.702
2000	36.752	30.860	11.5	5.142	9.44	21.905	30.860
2001	79.58	39.870	12.5	9.905	4.27	11.562	39.870
2002	93.822	37.802	14	9.847	4.665	10.792	37.802
2003	77	37.867	11	8.0265	2.045	10.555	37.867
2004	67.85	31.72	12	13.83	5.03	11.22	31.72
2005	69.25	36.56	2.63	22.24	0.56	12.075	36.56
2006	66.65	32.37	2.8935	7.59	0.785	14.87	32.37
2007	145	31.98	5.265	5.67	3.453	16.93	31.98

Earning per share, dividend per share and Return on equity were in increasing stage. Similarly price earning multiple was in satisfactory level. Earning yield is less increasing than above factors. Dividend yield were in decreasing stage in all years. Likewise market capitalization was also in decreasing stage in the late fiscal years. In the Fiscal year 2001/2002, market capitalization was in higher than late and early years.

A) Analysis of Data

The multiple correlation of above table has been done to analyze higher relationship of their dependent and independent variables. According to their relationship the higher correlation factors (positive and negative) are selected for multiple regression analysis.

Table 4.16

Multiple Correlations of the Time Series Data

		MC	EPS	DPS	PE	DY	EY	ROE
Column1	MC	1.000						
Column2	SPS	.695	1.000					
Column3	DPS	.873	.710	1.000				
Column4	PE	.085	-.447	.110	1.000			
Column5	DY	.017	-.361	-.367	-.073	1.000		
Column6	EY	-.004	.628	.274	-.350	-.820	1.000	
Column7	ROE	.695	1.000	.710	-.447	-.361	.628	1.000

According to the above table Market Capitalization has higher negative correlation with earning yield, and positive correlation with Earning per share, Dividend per share and Return on equity. Similarly earning per share has positive correlation with Dividend per share, earning yield but has negatively correlated with price earning multiple as well as Dividend yield. Likewise, dividend per share has positive correlation with price earning multiple and return on equity. And dividend yield has negatively correlated with EY and ROE.

According to the higher relationship, employing elimination process chooses only five variables. That is why, earning per share, dividend per share, dividend yield, earning yield and Return on equity is selected for multiple regression analysis.

In summary output is found by employing 5 variables in the multiple regression analysis of 9-year time series data are.

Multiple R	.978
R Square	.957
Adjusted R square	.886
Standard errors	10.136
Observations	9

Multiple R is 97.8%. Adjusted R Square of 9 observations is equal to 88.6%. It states that market capitalization is caused to change 88.6% by those independent variables. Rests of the other variables have less impact on market capitalization i.e. 11.4%. R-square implies the percentage of relationship between these variables in 9 observations. R square is found out to be 95.7%. Similarly standard error indicates the sizes of the errors in sampling that have been made and also have accuracy of sample that has been estimated to use sample statistic to estimate the larger standard error. The population of the standard error of above nine observations is equal to 10.136.

Table 4.17

Coefficient and P-value of Five Variables

Predictors	Coefficient	Standard error	t-stat	p-value
Intercept	2.982	9.079	.328	.764
Variable X1	16.601	22.278	.745	.510
Variable X2	3.177	2.229	1.425	.249
Variable X3	-2.982	5.046	-.591	.596
Variable X4	-3.387	2.362	-1.434	.247
Variable X5	-14.877	21.755	-.684	.543

(X1 = EPS; X2=DPS; X3=DY; X4=EY; X5=ROE)

The regression equation of Five Variables is found to be: Calculated value:-2.306

Y = 2.982+ 16.6011X1+3.1774X2-2.982X3-3.387X4-14.877X5

(.764) (.410) (.249) (.596) (0.247) (.543)

B) Test of Hypothesis

Above table states that the ‘t’ value of Earning per share came to be 0.745. Since the calculated t-value is less than the tabulated value at 5% level of significance at 8 degree of freedom. The null hypothesis of Market capitalization is dependent of EPS is accepted. It states that there is significant positive relationship between market capitalization and EPS. The co-efficient value of X1 indicated that EPS has

significant positive impact in Market capitalization. The coefficient of EPS states that if EPS is increased by 1% market capitalization is decreased by 16.60%.

The DPS also found to be positively related to market capitalization. The positive co-efficient value of DPS and the t-value are respectively 3.177 and 1.425. Since calculated t-value is less that the tabulated value at 5% level of significance at 8 degree of freedom. Null hypothesis of Market capitalization is dependent to DPS is accepted. It also stated that is significant positive relationship between market capitalization and DPS of Insurance and Finance Companies of Nepal.

The Dividend Yield and Market Capitalization came to be significant positive relationship. The calculated t-value is -0.591 and the coefficient value is-2.982. It states that the percent decrease in each variable is caused to decrease the given amount in market capitalization.

Similarly, the negative co-efficient by -3.387 and calculated t-values -1.434 states that there is significant relationship between the value of firm and earning yield. The null hypothesis of market capitalization is independent of EY is rejected in 5% level of significant. It states that the percentage decrease in each variable is caused to decrease the given amount of Market Capitalization.

Likewise, t-static and co-efficient value of ROE are negative that -6.84 & -14.877 respectively. The null hypothesis of Market Capitalization is dependent to ROE is accepted. It implies that ROE has significant impact in Market Capitalization. The percentage decrease in ROE has positive impact in market capitalization.

The analysis shows that EPS, DPS, DY, EY and ROE are significant determinants of Market Capitalization. The Multiple co-efficient of correlation states that the relationship between Market capitalization as dependent variable and all independent variable are highly significant and 97% of the variation in Market

Capitalization is explained by the independent variables i.e. EPS, DPS, DY. EY & ROE.

4.4 Major Findings of the Study

From the analysis of the data collected form various sources following findings have been made.

a) Stock market is an important constituent to the development of capital market as well as economy. Nepalese capital market is least developed that in developed countries. Stock market development indicator shows that liquidity and turnover are at minimum level than industrial developed countries.

b) The development of institution relates to stock market are also not in satisfactory level. These institutions have reinvigorating role to development of stock market. The overall development of economy has positive impact on stock market activities. Due to slow growth in national economy, stock markets have also direct effects. Main stock market development indicators followed the economic development indicators. It implies that both are in developing stage.

c) There was a bearish tendency in stock market since 1999. Share Price of Most of the companies had gone down up to 2004. The NEPSE Index since 1999 to 2002 raised and since 2002 onwards it is in declining position except F/Y 2006/07. As compared to the preceding year market capitalization went up to Rs 96813.74 billion at mid July 2007 whereas paid capital had gone to Rs 20008.55 million. The paid up capital and market capitalization of the previous year were Rs 16771.84 million and Rs 61365.89 million respectively. The NEPSE Index moved up from 227.54 in 2006 to 386.83 at mid July 2007.

d) The data for the F/Y 2006/07 reveals that Commercial banks occupy the topmost position in terms of annual turnover, market capitalization and other

companies in terms of NEPSE Index. Finance and Insurance sector occupy second rank in terms of Market capitalization, Annual turnover and NEPSE Index. Manufacturing and processing Companies occupies third rank in terms of Annual turnover but in terms of Market capitalization other companies occupied third rank. The NEPSE Index started with 176.31 in mid July 1998 and moved up to 386.83 in mid July 2007.

e) Change in NEPSE index is an indicator of market risk and return, thus, Risk and return are important concept to investment analysis. Ignoring this concept, investor could no analyze investment opportunity appropriately. Market return from 1998 to 2004 was 11.60%. Market variance and coefficient of variance were 7.49% and 235.79% respectively. Regarding with average return, C.V. has tremendously increased, it implies that stock market has increasing risk.

f) The data for the F/Y 2006/07 reveals that Commercial banks occupy the topmost position in terms of annual turnover, market capitalization and other companies in terms of NEPSE index. Finance and Insurance sector occupy second rank in terms of Market capitalization, Annual turnover and NEPSE index. Manufacturing and processing companies occupies third rank in terms of Annual turnover but in terms of Market capitalization other companies occupied third rank. The NEPSE Index started with 176.31 in mid July 1998 and moved up to 386.83 in mid July 2007.

g) Banking Sector dominates the whole transaction of Nepal stock Exchange. 78.12% of the Annual turnover is covered by banking sector only, which indicate that, the investors confidence is basically on banking sector only. Similar is the case with market capitalization and paid up value (70.96 and 42.60 respectively). Therefore the fate of stock market depends on the performance of banking sector i.e. the whole index of NEPSE is driven by the single sector of Banks.

h) The overall market return of stock market has found increasing than last years. In FY 2003/04, the return was -34.66% due to cause of decreasing index and return was highly decreased in F/Y 2003/04 too (i.e. -9.96%). The overall average return was 11.60%. It states that the return of stock market is lower than Banking sectors covering 12.71% of average return. Due to higher return in minimum risk, the participation of people is also encouraging in stock market (Especially in banking sector)

i) The average return of banking sector is 12.71% and Coefficient of variation (CV) is 251.69%. The return of banking sectors has not found significant difference than overall return. So, null hypothesis is accepted due to low calculated t-value than tabulated value. All companies of banking sector have positive return. Similarly, the average return of Finance and insurance is 8.78% and coefficient of variegation (CV) is 171.72%. The risk associated with Finance and insurance sector is lower than banking sector. The return of Kathmandu Finance limited is higher than Annapurna Finance Company Limited but return of AFC is also satisfactory level. Like wise return of Premier insurance company limited is higher than United Insurance Company limited. All the companies of banking, finance and insurance sectors pay the return for shareholders around overall market return.

j) By analyzing dependent and independent variables of market capitalization of Banking Sectors, EPS has found significant positive relationship with market capitalization. Similarly DPS and DY have also found significant impact in market capitalization. Earning yield and ROE has found negative significant impact in Market capitalization.

k) Similarly in the case of Finance and Insurance sectors, EPS has found significant relationship with market capitalization. Similarly, DPS has also found significant positive impact with market capitalization. Likewise, DY, EY and ROE have found significant negative relationship with market capitalization.

CHAPTER -V

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Summary

In mid eighties, Nepal adopted the economies liberalization in order to channelize the scarce resources form local and foreign investment. Keeping in view the importance of capital market in economic development, policy maker started to give considerable attention to the development of capital market's regulation, change and improvement. Even though the concept of capital market was started in 1936 with formation of industrial council, the market got momentum only after the restoration of democracy in 1990. The adoption of open economy by the Government in 1992 encouraged the foreign and local investment. To regularize and systemize the capital market security Board and Nepal stock exchange was established in 1994.

There was bearish tendency in stock market since 1999. Share price of Most of the companies had gone down up to 2003. The NEPSE index since 1998 to 2001 raised and since 2001 onwards it is in declining position except F/Y 2006/07. As compared to the preceding year market capitalization went up to Rs 96813.74 billion at mid July 2007 whereas paid capital had gone to Rs 20008.55 million. The paid up capital and market capitalization of the previous year were Rs 16771.84 million and Rs 61365.89 million respectively. The NEPSE Index moved up from 227.54 in 2007 to 386.83 at mid July 2007.

It is important to have adequate capital for the development of the country, public organization as well as private organization equally needs this scarce resource to enhance their business. Short-term source of fund is not always adequate for the successful operation of business. In the crux of this the concept of capital market

was developed in which scattered and unproductive funds are channelized to the productive sector.

The data for the F/Y 2006/07 reveals that commercial banks occupy the topmost position in terms of annual turnover, market capitalization and other companies in terms NEPSE Index. Finance an Insurance sector occupy second rank in terms of Market capitalization, Annual turnover and NEPSE Index. Manufacturing and processing companies occupies third rank in terms of Annual turnover but in terms of Market capitalization other companies occupied third rank. The NEPSE Index started with 176.31 in mid July 1998 and moved up to 386.83 in mid July 2007.

Change in NEPSE index is an indicator of market risk and return, thus, Risk and return are important concept to investment analysis. Ignoring this concept, investors could no analyze investment opportunity appropriately. Market return from 1997 to 2003 was 11.60%. Market variance and coefficient of variance were 7.49% and 235.79% respectively. Regarding with average return, C.V. has tremendously increased, it implies that stock market has increasing risk.

Comparing the return of each sector, return of Hotels sectors in these period show -2.89% due decrease in NEPSE index and injuriously affected tourism in Nepal since Maoist revolution started in the country. Other sector is higher than other sectors i.e. 25.98%. Return of trading sector is very low i.e. 0.39%. Return of Manufacturing and processing companies remain at 7.75%. Similarly, Return of Banking and Finance and insurance are 12.71% and 8.78% respectively. In the yearend 2006 the overall market return was positive i.e. 34.93% due to increase of NEPSE index of each sector expect hotels sector. That's why the study shows there is low opportunity for the individual as well as institutional investors for secondary trading. The stock of Banking, Finance and Insurance companies have able to generate up to overall market return. However, return of Finance and

Insurance sector is associated with lower risk in comparison to banking sector. The coefficient of variation of Finance and Insurance sector has 171.72% where as 251.69% banking sectors.

The average returns of sample companies are associated with positive return. All of the companies of Banking, Finance and Insurance have generated profit to stockholders. As our study shows what the Banking sectors are distributing more dividends (Cash dividend as well as stock dividend) than Finance and insurance companies. The expected average returns of stock investment Bank of Kathmandu Ltd. Was higher (82.85%) than other banks on the period under study 1998-2007. The lowest return among banks in Nepal SBI Bank Ltd. (18.47%). And the rest of banks have satisfied average return. In the case Finance companies, Kathmandu Finance limited was higher return (i.e. 40.38%) than Annapurna Finance Company. But the AFC return was also good (i.e. 32.06%). The return of premier insurance company (11.95%) limited was higher (i.e. 12.68) than united insurance company.

The hypothesis was also tested to compare individual return of each company as well as sectoral return to overall market return. Out of them sectoral return of Banking, Finance and Insurance companies have not found significant difference to overall market return. These sectors are able to pay stockholders around overall market return. Similarly, return of individual companies of Banking, finance and insurance are not found any significant difference to overall market.

Earning per share, Dividend per share, Dividend Yield were in fluctuation stage. Increasing and decreasing stage in the corresponding fiscal years. Price earning ration is in increasing stage. Earning yield and Return on equity increased less than above factors. Market capitalization was in decreasing stage. In the fiscal year 2000/2001, Market capitalization was higher than late and early year till the F/Y

2002/03. Now it is increasing way. Due to high earning per share and high DPS, whether the listed numbers of share are higher, Market capitalization were average in all year and also the return of all the companies of Banking, Finance and Insurance were positive.

In the case of Banking Sectors, EPS has found significant positive relationship with market capitalization. Similarly DPS and DY have also found significant impact in market capitalization. Earning yield and ROE has found negative significant impact in Market capitalization.

Similarly in the case of Finance and Insurance sectors, EPS has found significant relationship with market capitalization. Similarly, DPS has also found significant position impact with market capitalization. Like wise, DY, EY and ROE has found significant negative relationship with market capitalization.

5.2 Conclusion

Stock market is an important constituent to the development of capital market as well as economy. Nepalese capital market is least developed that in developed countries. Stock market development indicator shows that liquidity and turnover are at minimum level than industrial developed countries.

The development of institution relates to stock market are also not in satisfactory level. These institutions have reinvigorating role to development of stock market. The overall development of economy has positive impact on stock market activities. Due to slow growth in national economy, stock markets have also direct effects. Main stock market development indicators followed the economic development indicators. It implies that both are in developing stage.

The data for the F/Y 2006/07 reveals that Commercial banks occupy the topmost position in terms of annual turnover, market capitalization and other companies in terms of NEPSE index. Finance and insurance sector occupy second rank in terms of Market capitalization, Annual turnover and NEPSE index. Manufacturing and processing Companies occupies third rank in terms of Annual turnover but in terms of Market capitalization other companies occupied third rink. The NEPSE index started with 176.31 in mid July 1997 and moved up to 386.83 in mid July 2007.

Banking sector dominates whole transaction of Nepal stock 78.12% pf the Annual turnover is covered by banking sector only, which indicate that, the investors confidence is basically on banking sector only. Similar is the case with market capitalization and paid up value (70.96 and 42.60 respectively). Therefore the fate of stock market depends on the performance of banking sector i.e. the whole index of NEPSE in driven by the single sectors of Banks.

The overall market return of stock market has found increasing than last years. In FY 2003/2004 the return was -34.66% due to cause of decreasing index and return was highly decreased in F/Y 2003/2004 (i.e. -9.96%). The overall average return was 11.60%. It states that the return of stock market is lower than Banking sectors covering 12.71% of average return. Due to higher return in minimum risk, the participation of people is also encouraging in stock market (Especially in banking sector)

The average return of banking sector of 12.71% and Coefficient of variation (CV) is 251.69%. The return of banking sectors has not found significant difference than overall return. So, null hypothesis is accepted due to low calculated t-value than tabulated value. All companies of banking sector have positive return. Similarly, the average return of Finance and insurance is 8.78% and coefficient of variation

(CV) is 171.72%. The risk associated with Finance and insurance sector is lower than banking sector. The return of Kathmandu finance limited is higher than Annapurna Finance Company limited but the return of AFC is also satisfactory level. Like wise return of premier insurance company limited is higher than United Insurance Company limited. All the companies of banking, finance and insurance sectors pay the return for shareholders around overall market return.

By analyzing dependent and independent variables of market capitalization of Banking Sectors, EPS has found significant positive relationship with market capitalization. Similarly DPS and DY have also found significant impact in market capitalization. Earning yield and ROE has found negative significant impact in Market capitalization.

Similarly in the case of Finance and Insurance sectors, EPS has found significant relationship with market capitalization. Similarly, DES has also found significant positive impact with market capitalization. Likewise, DY, EY and ROE have found significant negative relationship with market capitalization.

5.3 Recommendations

The recommendation of this study is the important information for those who are very much concerned directly with the valuation of stock. Thus, following recommendation and suggestion can be outlined.

i. The coefficient of variation of banking sector is higher than Finance and insurance sector under this study period. Stability in service, earning and profits are major indicators to minimize the fluctuation of market return. Specially, banking sectors should concern to maintain the stability in services, earning and profits.

ii. Under the study period of 1998 to 2007, the Risk associated with banking sector is higher than insurance and finance sectors. Thus it is recommended

to make stable dividend policy that can minimize risk. And also it is recommended to construct portfolio between the Banking, Finance and Insurance sectors to diversify risk and maximization of return.

iii. Earning per share and Dividend per share of Banking sector and Earning per share, Dividend per share of Finance and Insurance sector have found positive impact in market capitalization. Thus, this sort of parameter should be maintained regularly to reduce negative impact in market value of firm.

iv. Earning yield and return on equity of Banking sector as well as dividend yield, earning yields and return on equity of Finance and Insurance sectors are negatively correlated. The parameters that affect the market capitalization of firm should be considered in order to increase the market capitalization.

v. Most of the individual invertors are revealed to be isolated and incapable to analyzing the performance of the company in which they have invested. Therefore for the effective and efficient investment decision on securities, professional advisory institution should create the appropriate atmosphere to the willing investors by awaiting capital market investment and information.

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