CHAPTER – I

INTRODUCTION

1.1 Background of the Study

Securities, in finance, are the instruments which give their legal holders rights to money or other property. In other words, securities are documents that represent an interest or a right in something else; they are not consumed or used in the same way as traditional consumer goods. Securities include stocks, bonds, notes, mortgages, bills of lading, and bills of exchange. Similarly, a security trading is the financial activity involving transactions of property such as stocks, bonds, commodities, and currency.

Companies issue new securities in what is known as the primary market, usually with the help of investment bankers. In other words, primary market for securities is the new issues market which brings together the "supply and demand" or "sources and uses" for new capital funds. The investment bank acquires the initial issue of the new securities from the company at a negotiated price and then makes the securities available for its clients and other investors in an initial public offering. In this primary market, company receives the proceeds of security sales. After this initial offering, the securities are bought and sold in the secondary market. Moreover the purpose of a stock exchange or secondary securities market, like any other organized market, is to enable buyers and sellers to effect their transactions more quickly and cheaply than they could otherwise. Securities are often listed in a stock exchange, an organized and officially recognized market on which securities can be bought and sold. Issuers may seek listings for their securities in order to attract investors, by ensuring that there is a liquid and regulated market in which investors will be able to buy and sell securities.

The total capital of the company is divided into several units and each unit is a security. These securities are not liquid assets unless they find the place to

trade. Hence, a place is designed where buyer and seller meets and securities are traded. The system that provides liquidity to the securities is termed as Security Trading System and the place is the Stock Exchange Centre.

The stock exchanges provide liquidity to the investors who provide funds for the establishment of the productive enterprises. The stock exchanges also encourage the savers to save more and the enterprising economic units to start productive ventures. Stock exchanges, the organized market for buying and selling financial instruments (known as securities) like stocks, bonds, options, etc, have specific locations where the trades are completed. Exchanges operate as the action markets-buy and sell orders come in more or less simultaneously, and exchange members match these orders. The company is not usually involved in the trading of its stock in the secondary market, the essential function of stock exchanges. By providing investors the opportunity to trade financial instruments, the stock exchanges support the performance of the primary markets. This arrangement makes it easier for companies to raise the funds that they need to build and expand their businesses.

The basic functions of stock exchange are to provide and allocate capital funds to the firms with profitable investment opportunities and to offer an avenue of liquidity for individuals to invest current income or borrow against future income and thereby achieve their preferred time pattern consumption. Because investing involves uncertainty, stock exchanges provide a means for transferring risk among the parties to these transactions. The stock exchanges and the economy move in similar cyclical patterns. Although some analysts view stock markets in developing countries as 'casinos' that have little positive impact on economic growth, recent evidences suggest that stock exchanges can give a big boost to economic development for the developing countries like Nepal.

1.2 Statement of the Problem

Realizing the importance of securities exchange center as a secondary market of securities and stock, various studies have been undertaken regarding the performance of them. Stock market is the secondary market which embraces buyers and sellers who meets with their specific requirements. Stock exchanges put finger on the pulse of the economy and give the diagnosis to the public in the form of quotation.

The research conducted so far has found that major problems seen in the system are; ambiguities in the regulations, inadequate legal provisions, inadequate market infrastructure, lack of clear demarcation of the regulators, poor corporate cultures, lack of willingness among the corporate sector to disseminate the fair and timely information, lack of professionalism of the market participants, lack of awareness among the investors, lack of self-consciousness investors, lack of providing fair return on investment to investors, etc. Observing these various problems in the NEPSE, this study is therefore, devoted towards examining the present condition of the stock trading system in NEPSE. Specifically, the main issues of the study are as follows:

a. How many companies are listed in NEPSE and how many, out of them, are able to transact their securities?

b. What are the annual trend and the current situation of turnover, market capitalization and NEPSE index?

c. Which sectors' securities are traded most?

d. What are the current conditions of share price and the turnover (amount traded) of the securities of companies listed in NEPSE?

e. Does the share price correlate with turnover of the companies?

f. What role can NEPSE play for the overall development of the economy?

g. What are the future predictions regarding the different aspects of NEPSE?

h. What should be done for the systematic growth of securities market in Nepal?

1.3 Objectives of the Study

The main objective of the research is to examine the securities market in Nepal. However, the specific objectives of the study are as follows:

a. To analyze the trend of securities trading in NEPSE.

b. To assess the financial perspective of securities trading in Nepal.

c. To estimate the value of the NEPSE index, market capitalization and turnover in future.

d. To trace out the problem and prospects of securities market.

1.4 Significance of Study

The study is concerned to the theoretical explanation and practical application of securities market of listed companies in Nepal. The study might be valuable for investors, as it examines the trend of securities in NEPSE and the problems and prospects of securities market, for collecting the securities related information. Besides them, the study will be equally significant to the SEBON and NEPSE personnel for formulating appropriate rules and regulations that will robust the securities transaction system. Further, the study will be also beneficial to the listed companies to gain idea on the securities trading. Eventually, the study will be crucial to the researchers to have knowledge on securities trading.

1.5 Limitations of the Study

The study mainly focuses on the securities trading of listed companies. Due to the limited time and resource to conduct the study, it does have some limitations.

a. The research is confined to the activities of NEPSE and so is dependent on the data provided by the NEPSE and SEBON.

b. No attempts are made to examine the reliability of the available secondary data since they are officially released by the related authorities.

c. The non-availability of required data and references are also one of the limitations of the study.

d. The reliability of the primary data depends totally on the opinion of the respondents.

e. The study covers securities trading of five year only, i.e. from the fiscal year 2004/05 to 2008/09.

1.6 Organization of the Study

Following a simple research methodology approach, this study is organized under five different chapters. The title and brief sketch of each chapter is as follows:

Chapter-I: It contains the introduction of the study where it includes background of the study, statement of the problem, objective of the study, significance of the study, limitations and organization of the study.

Chapter-II: It incorporates theoretical framework and review of the articles, journals and past researches and other empirical studies conducted inside and outside the country.

Chapter-III: It explains the methodology used in the research to arrive at the results in the context of arriving at the objective of the study. It therefore basically deals with the nature and sources of data, research design, method of data collection and statistical tools and techniques used in analysis of data.

Chapter -IV: It deals with the analysis of primary and secondary data collected during the study by using different tools and methods and scoring empirical findings out of the study.

Chapter-V: It covers summary, conclusions and recommendations of the study followed by appendices and bibliographical references.

CHAPTER – II
REVIEW OF LITERATURE

2.1 Conceptual Framework

2.1.1 Securities Market

"Securities market is an economic institute within which take place sale and purchase transactions of securities between subjects of economy on the base of demand and supply. Also we can say that securities market is a system of interconnection between all participants (professional and nonprofessional) that provides effective conditions: to buy and sell securities,

) to attract new capital by means of issuance new security (securitization of debt),

) to transfer real asset into financial asset,

) to invest money for short or long term periods with the aim of deriving profit." *(Noussair, Robin and Ruffieux; 1998: 61)*

"A security market can be defined as a mechanism of bringing together buyers and sellers of financial assets in order to facilitate trading. Alternatively, security market is a place of places where securities are bought and sold, the facilities and people engaged in such transactions, the demand for and availability of securities to be traded, and the willingness of buyers and sellers to reach agreement on sales." *(Freedman: 1999; 47)*

Although, securities markets are concentrated in few locations, they refer more to mechanism, rather than to place, designed to facilitate the exchange of securities by bringing buyers and sellers of securities together. In other words, people and organizations wanting to borrow together with those having surplus funds in the securities markets. "Securities, such as equities, short and long term debt instruments, derivatives etc are the products that are traded in the markets, institutions such as investment bankers and security firms, securities issuing institution such as government and corporate bodies and the

participants of the securities markets. Securities markets' major function is to provide line between saving and investment there by facilitating the creation of new wealth." *(Pastor and Stambaugh; 2003: 132)*

2.1.2 Functions of Securities market

The common market functions of securities market;

- ∫ commercial function (to derive profit from operation on this market)
- ∫ Price determination (Demand and Supply balancing, the continuous process of prices movements guarantees to state correct price for each security (So, the market corrects mispriced securities)
- ∫ Informative function (market provides all participants with market information about participants and traded instruments)
- ∫ Regulation function (securities market creates the rules of trade, contention regulation, priorities determination)

Specific functions of the securities market;

- ∫ Transfer of ownership (securities markets transfer existing stocks and bonds from owners who no longer desire to maintain their investments to buyers who wish to increase those specific investments. There is no net change in the number of securities in existence, for there is only a transfer of ownership. The role of securities market is to facilitate this transfer of ownership. This transfer of securities is extremely important, for securities holders know that a secondary market exists in which they may sell their securities holdings. The ease with which securities may be sold and converted into cash increases the willingness of people to hold stocks and bonds and thus increases the ability of firms to issue securities)
- ∫ Insurance (hedging) of operations though securities market (options, futures)

2.1.3 Levels of Securities market

A) Primary market

"The <u>primary market</u> is that part of the capital markets that deals with the issue of new securities. Companies, governments or public sector institutions can obtain funding through the sale of a new stock or bond issue. This is typically done through a syndicate of securities dealers. The process of selling new issues to investors is called underwriting. In the case of a new stock issue, this sale is an initial public offering (IPO). Dealers earn a commission that is built into the price of the security offering, though it can be found in the prospectus. Primary markets creates long term instruments through which corporate entities borrow from capital market." *(Mankiw and Zeldes; 1991: 57)* Features of primary markets are:

- ʆ This is the market for new long term equity capital. The primary market is the market where the securities are sold for the first time. Therefore it is also called the new issue market (NIM).
- ʆ In a primary issue, the securities are issued by the company directly to investors.
- ʆ The company receives the money and issues new security certificates to the investors.
- ʆ Primary issues are used by companies for the purpose of setting up new business or for expanding or modernizing the existing business.
- ʆ The primary market performs the crucial function of facilitating capital formation in the economy.
- ʆ The new issue market does not include certain other sources of new long term external finance, such as loans from financial institutions. Borrowers in the new issue market may be raising capital for converting private capital into public capital; this is known as "going public."
- ʆ The financial assets sold can only be redeemed by the original holder.

Methods of Issuing Securities in the Primary Market are:

- Initial public offering;
- Rights issue (for existing companies);
- Preferential issue.

B) Secondary Market

"The secondary market, also known as the aftermarket, is the financial market where previously issued securities and financial instruments such as stock, bonds, options, and futures are bought and sold. The term "secondary market" is also used to refer to the market for any used goods or assets, or an alternative use for an existing product or asset where the customer base is the second market (for example, corn has been traditionally used primarily for food production and feedstock, but a 'second' or 'third' market has developed for use in ethanol production).

With primary issuances of securities or financial instruments, or the primary market, investors purchase these securities directly from issuers such as corporations issuing shares in an IPO or private placement, or directly from the federal government in the case of treasuries. After the initial issuance, investors can purchase from other investors in the secondary market." *(Black; 2001: 123)*

The secondary market for a variety of assets can vary from loans to stocks, from fragmented to centralized, and from illiquid to very liquid. The major stock exchanges are the most visible example of liquid secondary markets - in this case, for stocks of publicly traded companies. Exchanges such as the New York Stock Exchange, Nasdaq and the American Stock Exchange provide a centralized, liquid secondary market for the investors who own stocks that trade on those exchanges. Most bonds and structured products trade "over the counter," or by phoning the bond desk of one's broker-dealer. Loans sometimes trade online using a Loan Exchange.

C) Over-the-counter market

"An over-the-counter contract is a bilateral contract in which two parties agree on how a particular trade or agreement is to be settled in the future. It is usually from an investment bank to its clients directly. Forwards and swaps are prime examples of such contracts. It is mostly done via the computer or the telephone. For derivatives, these agreements are usually governed by an International Swaps and Derivatives Association agreement.

Over-the-counter (OTC) or off-exchange trading is to trade financial instruments such as stocks, bonds, commodities or derivatives directly between two parties. It is contrasted with exchange trading, which occurs via facilities constructed for the purpose of trading (i.e., exchanges), such as futures exchanges or stock exchanges." *(Yartey; 2006: 17-18)*

2.1.4 Main Financial Instruments

Bond, Promissory note, Cheque – a security contains requirement to make full payment to the bearer of cheque , Certificate of deposit, Bill of Lading (a Bill of Lading is a "document evidencing the receipt of goods for shipment issued by a person engaged in the business of transporting or forwarding goods."

A) Promissory note

"A promissory note, referred to as a note payable in accounting, or commonly as just a 'note', is a contract where one party (the maker or issuer) makes an unconditional promise in writing to pay a sum of money to the other (the payee), either at a fixed or determinable future time or on demand of the payee, under specific terms. They differ from IOUs in that they contain a specific promise to pay, rather than simply acknowledging that a debt exists." *(Doodh; 1962; 110)*

B) Certificate of Deposit

"A <u>certificate of deposit</u> or CD is a time deposit, a financial product commonly offered to consumers by banks, thrift institutions, and credit unions. CDs are similar to savings accounts in that they are insured and thus virtually risk-free; they are 'money in the bank' (CDs are insured by the FDIC for banks or by the NCUA for credit unions). They are different from savings accounts in that the CD has a specific, fixed term (often three months, six months, or one to five years), and, usually, a fixed interest rate. It is intended that the CD be held until maturity, at which time the money may be withdrawn together with the accrued interest." *(Kene; 1983: 35)*

C) Bond

"<u>Bond</u> - an issued security establishing its holder's right to receive from the issuer of the bond, within the time period specified therein,

)   its <u>nominal value</u>

)   and the interest fixed therein on this value or other property equivalent.

The bond may provide for other property rights of its holder, where this is not contrary to legislation." *(Rao; 1988: 74)*

D) Bill of Lading

"A <u>bill of lading</u> (sometimes referred to as a BOL,or B/L) is a document issued by a carrier to a shipper, acknowledging that specified goods have been received on board as cargo for conveyance to a named place for delivery to the consignee who is usually identified. A thorough bill of lading involves the use of at least two different modes of transport from road, rail, air, and sea. The term derives from the verb "to lade" which means to load a cargo onto a ship or other form of transportation." *(Sur; 1980: 29)*

E) <u>Stocks</u> (<u>Shares</u>)

a) Common Shares

"<u>Common Shares</u> represent ownership in a company and a claim (dividends) on a portion of profits. Investors get one vote per share to elect the board members, who oversee the major decisions made by management. Over the long term, common stock, by means of capital growth, yields higher returns than almost every other investment. This higher return comes at a cost since common stocks entail the most risk. If a company goes bankrupt and liquidates, the common shareholders will not receive money until the creditors, bondholders, and preferred shareholders are paid." *(Edward and Magee; 1998: 161-162)*

b) Preferred Stock

"<u>Preferred Stock</u> represents some degree of ownership in a company but usually doesn't come with the same voting rights. (This may vary depending on the company.) With preferred shares investors are usually guaranteed a fixed dividend forever. This is different than common stock, which has variable dividends that are never guaranteed. Another advantage is that in the event of liquidation preferred shareholders are paid off before the common shareholder (but still after debt holders). Preferred stock may also be callable, meaning that the company has the option to purchase the shares from shareholders at anytime for any reason (usually for a premium). Some people consider preferred stock to be more like debt than equity. A good way to think of these kinds of shares is to see them as being in between bonds and common shares." *(Edward and Magee; 1998: 165)*

2.1.5 Professional Participants in Securities Market

Professional participants in the securities market - legal persons, including credit organizations, and also citizens registered as business persons who conduct the following types of activity:

A) **Brokers**

"Brokers are the agents or middlemen, who facilitate the buying and selling of securities for investors. They take buy or sale orders from the investors in their own office and executes the transactions in the floor of the exchange. Besides the basic service of executing orders, brokers also provide services such as holding securities for safe keeping, providing information and advice relating to investment alternatives, extending margin loans and facilitating short sales." *(Thygerson; 1992: 132)*

B) **Dealers**

"Dealers trade solely for themselves and are prohibited from handling public orders. Since dealers have access on the floor and can own securities on their own name, they benefit from buying at low and selling at high prices. The benefit of the dealers to the market is that their buy and sell actions added up liquidity of the securities." *(Thygerson; 1992: 132)*

C) **Market Makers**

"Market makers, also known as specialists, facilitate the trading of securities by maintaining inventory in particular securities. They are similar to dealers in many ways except that they always stand ready to buy and sell securities at their bid and asked price for which they are market maker." *(Thygerson; 1992: 133)*

2.1.6 Securities Market and Economic Growth

"The securities market fosters economic growth to the extent that it-(a) augments the quantities of real savings and capital formation from any given

level of national income, (b) increases net capital inflow from abroad, (c) raises the productivity of investment by improving allocation of investible funds, and (d) reduces the cost of capital.

It is reasonable to expect savings and capital accumulation and formation to respond favorably to developments in securities market. The provision of even simple securities decouples individual acts of saving from those of investment over both time and space and thus allows savings to occur without the need for a concomitant act of investment. If economic units rely entirely on self-finance, investment is constrained in two ways: by the ability and willingness of any unit to save, and by its ability and willingness to invest. The unequal distribution of entrepreneurial talents and risk taking proclivities in any economy means that at one extreme there are some whose investment plans may be frustrated for want of enough savings, while at the other end, there are those who do not need to consume all their incomes but who are too inert to save or too cautious to invest the surplus productively. For the economy as a whole, productive investment may thus fall short of its potential level. In these circumstances, the securities market provides a bridge between ultimate savers and ultimate investors and creates the opportunity to put the savings of the cautious at the disposal of the enterprising, thus promising to raise the total level of investment and hence of growth." *(Kiley; 2000: 47-48)*

The securities market facilitates the internationalization of an economy by linking it with the rest of the world. This linkage assists through the inflow of capital in the form of portfolio investment. Moreover, a strong domestic stock market performance forms the basis for well performing domestic corporate to raise capital in the international market. This implies that the domestic economy is opened up to international competitive pressures, which help to raise efficiency. It is also very likely that existence of a domestic securities market will deter capital outflow by providing attractive investment opportunities within domestic economy. A developed securities market

successfully monitors the efficiency with which the existing capital stock is deployed and thereby significantly increases the average return.

In as much as the securities market enlarges the financial sector, promoting additional and more sophisticated financing, it increases opportunities for specialization, division of labor and reductions in costs in financial activities. The securities market and its institutions help the user in many ways to reduce the cost of capital. They provide a convenient market place to which investors and issuers of securities go and thereby avoid the need to search a suitable counterpart.

There are also other developmental benefits associated with the existence of a securities market. First, the securities market provides a fast-rate breeding ground for the skills and judgment needed for entrepreneurship, risk bearing, portfolio selection and management. Second, an active securities market serves as an 'engine' of general financial development and may, in particular, accelerate the integration of informal financial systems with the institutional financial sector. Securities directly displace traditional assets such as gold and stocks of produce or, indirectly, may provide portfolio assets for unit trusts, pension funds and similar FIs that raise savings from the traditional sector. Third, the existence of securities market enhances the scope, and provides institutional mechanisms, for the operation of monetary and financial policy. While the above indicate that the securities market promotes economic growth, it is not one way relation. The economic growth also promotes securities market.

2.1.7 Problems of Securities Growth

As in most nascent markets, Nepal also went through a volatile period in its early years. In the section above, three market factors were identified whose dynamics influence the market behavior. Given below is a discussion on some

of the problems faced in each of these three areas, especially during the speculative market stage.

2.1.7.1 Lack of Tradable Market Instruments

"Tradable market instruments in Nepal are limited to equity shares. An alternate over the counter market existed for long-term government bonds. However, during the initial speculative period, bank interest rates were at their all-time low, with Treasury bill rates in the range of 4.5%. Since bond trading was done at par, investors held on to their bonds and this market was very stagnant. Moreover, as interest rates on commercial bank deposits were very low, investor interest in the stock market was quite high as a higher return investment option. In the absence of alternative investment opportunities, the demand of shares built up heavily. This was particularly problematic in the initial speculative period, as it only fueled the price rise of already overvalued shares." *(Finnerty; 1996: 62)*

2.1.7.2 Market Intermediaries and Investors

a) An Oligopolistic Market Structure

In its early stages, the market had very few active members. There were 25 registered stock brokers of whom only about 10 were active. There were only 3 market makers. As a result of this oligopolistic structure, prices could easily be manipulated with very small transactions. This easily led to transactions being made on a speculative basis rather than on an investment basis. Similarly, when the market makers realized that they could exert tremendous market power, rather than playing a stabilizing role by trading on the basis of company's underlying financial position, the market makers themselves made transactions on a speculative basis which pushed the prices up further.

b) Functional Overlaps Amongst Intermediaries

Because of low business volumes, financial intermediaries such as merchant banks and brokers become engaged in multiple functioning, which according to developed country standards would constitute severe conflicts of interest. For instance, in Nepal, a market maker could also operate as a portfolio manager and a mutual fund manager. Similarly, auditors are also working as brokers. Some market makers are also sitting on the Board of Directors of listed Companies. Most interestingly, even regulators are directors of some of the market intermediaries. This is one of the glaring problems existing in Nepal which lends itself to insider information problems and conflicts of interest.

2.1.7.3 Economic and Regulatory Environment

a) Insufficient Scrips

"One of the most common problems in emerging markets is the scarcity of public companies. Typically in developing countries, business enterprises are small in nature, closely held usually within a family and are highly reluctant to go public. This hesitation usually stems from the fear of making their financial statements public, thus no longer being hidden from tax authorities. This is, by far, one of the biggest reasons in deterring private businesses from going public. Similarly, dealing with shareholders - most of whom are not well educated - is rather cumbersome to promoters. They also fear the loss of control to outsiders. In developing countries, where information is so scarce, businesses fear sharing this information to outsiders, especially competitors. Well established businesses have very strong relationships with commercial banks who will happily cover their financial needs. Hence, the need to resort to capital markets is less. As a result, the supply of shares in the stock market is limited." *(Ludvigson and Steindel; 1996: 42)*

b) Competition with the Financial Sector

"The growth of the capital market is intricately related to the state of financial markets such as the banking sector and government bond market. Usually, the

banking sector plays a competitive role in the development of capital markets." *(Ludvigson and Steindel; 1996: 43)* In Nepal, while the banking sector was crucial in developing the capital market, the banking sector also plays a strong complementary role in fulfilling financial needs of businesses. Share markets are resorted to only when it is mandated by a government directive or if the company leverage has reached very high levels.

c) Regulatory Confusion

In Nepal, a Universal Banking modality has been followed. Under this system, deposit taking institutions such as commercial banks and finance companies are also allowed to participate in the capital markets. Since these institutions are regulated by the Central Bank as well as the Securities Exchange Board, the presence of multiple regulators adds to the confusion. A striking example of this is the approval for operation of a mutual fund by the Central Bank even before the establishment of the Securities Exchange Board. In the absence of a coordinated effort whereby these institutions regulate by function rather than by institution, the enforcement capacity of these organizations is heavily undermined.

d) Enforcement

Perhaps the biggest problem that emerged in the capital markets in Nepal is the lack of teeth of the enforcement agencies. This can be attributed to several factors:

i. Inadequate Legal System: The Securities Exchange Act lacks clarity in terms of the regulatory purview of the Securities Board over the market intermediaries. It does not vest sufficient powers on the Board to issue and enforce the rules and guidelines. Rules and Regulations can only be issued with the approval of the Cabinet. More than four years after the Board's establishment, this has yet to be amended. Another example of this weak legal infrastructure has been the outdated Companies Act. This Act is yet to be amended to include the information reporting standards and accounting

standards required for publicly traded companies and timely ownership transfers to ensure liquidity in such a market.

ii.Fear of Regulatory Overkill: Market intermediaries are usually few in number and are engaged in multiple activities. At this infancy stage, regulators are constantly plagued with the dilemma of acting as a market promoter versus a market regulator. Regulators are worried of an "overkill" which may have a ripple effect in terms of investor confidence. This often results in extended forbearance with detractors. In a non-competitive, nascent market, regulators are often unable to enforce rules strictly. The NCM Mutual Fund is a typical case in point.

iii. Ownership: A unique problem for proper enforcement in Nepal has been the ownership structure of institutions in Nepal. The Nepal Stock Exchange, instead of being owned by brokers, is still owned by the Central Bank, Government and a semi-government enterprise, the Nepal Industrial Development Corporation. Hence, the Stock Exchange has yet to emerge as a self-regulatory body.

The overlapping of institutional ownership has also undermined the regulatory capacity of the institutions. For example, Citizen's Investment Trust, a licensed intermediary under its own Act, which was promoted by the Securities Exchange Center, is today in direct competition with other private sector intermediaries in areas such as primary issues, fund management, and market making. The Executive Director of this company is the Executive Chairman of the Securities Exchange Board - a regulatory body. Such conflicts of interest and overlapping of roles has greatly undermined the credibility of the regulatory authoritative body in Nepal.

2.1.8 Malpractices in Share Market

Various irregularities exist in Nepal's Share Market. Although these irregularities generate income to certain group, general investor suffers from this. To build clear and transparent share market, the individual and institution, who inspect share market, should always remain aware. The irregularities that exist in Nepal's Share Market are:

2.1.8.1 Pooling

"In this irregularity, a certain group buys and sales share of certain company within themselves in order to raise up the price of share by displaying the maximum number of shares transaction to the general public. And when the price reaches its zenith, the pooling members sells the shares and the share price, which rose up unnecessarily without any specific basis declines as a result the general investors, who buys that share with the hope of price rise, have to bear a great loss." *(Bhattarai; 2006: 28)*

2.1.8.2 Cornering or Warehousing

"The individual or group involved in this irregularity buys all the shares of certain company. As a result, the share of such company is limited to a single person or group and invites scarcity of share of such company. The supply of such share becomes low and demand will be high. On the increased demand of share, the person or group involved in cornering or warehousing sells in small lot, takes the share price to the maximum height and sells the remaining shares in high price." *(Bhattarai; 2006: 28)*

2.1.8.3 Organized Runs

"In organized runs, an active group flows an unnecessary rumor of certain company to influence share price. The main objective to flow such rumor is to fascinate the investor in the share and to sell the shares of the individual doing

organized transactions. Both capital gain and prompt sale are achieved from this organized runs." *(Bhattarai; 2006: 28)*

2.1.8.4 Ramping

"To attract investors by displaying fast transactions of the shares dramatically just before the last movement of share transactions in the market and to make profit from such runs is ramping. From this fast raising of share price, the general investor guess that the demand for that company's share is high and will increase further in future." *(Bhattarai; 2006: 29)*

2.1.8.5 Washsale

"Washsale is not actually a sale of share. Actually, the person involved in it sales shares to his family and relatives and indicates that the share price of certain is in decreasing/increasing. In this, the person sells share to himself in low price and indicates the price fall in the market and finally buys the share in low price to reap profit. The person involved in this does such activity with the aid of broker." *(Bhattarai; 2006: 29)*

2.1.8.6 Matching

"If a same broker gets both selling and buying order, then matching can occur. The broker may decrease the price if he is closer to buyer and may increase the price if he is closer to seller to match the order." *(Bhattarai; 2006: 30)* However, this kind of activity has been prohibited from Ashad 2062 B.S.

2.1.8.7 Insider Training

"The transaction done with the aid of confidential information of company is called Insider Trading. On the basis of unpublished information especially if the company's staff, director or executive takes advantages by buying/selling the share of same company, then it is called Insider Trading. For example, if the board of directors decides to distribute dividend but such decision has not been publicized and on the basis of this decision, the decision maker and other company staff, knowing the decision, collects the share of the company and

sells after the price increment or takes the bonus share, then this kind of transaction is known as Insider Training." *(Bhattarai; 2006: 30)*

2.1.9 Prospects of Nepal's Stock Market

The amendment in the securities exchange act and the guidelines were some of the measure taken to improve in the legal and statutory Framework. Nowadays, different measures have been taken to improve the performance of stock market and all the improvement activities will be prospects of Nepalese Stock Market, which are given below:

2.1.9.1 Trading System Automated

The Automated Trading System (ATS), an internationally compatible trading system was inaugurated by the then Finance Minister Dr. Ram Sharan Mahat on 24 August 2007. In order to adopt the ATS, NEPSE made an agreement with the British Company Comdaq Limited in November 2006 under the Asian Development Bank (ADB) loan assistance project--Corporate and Financial Governance (CFG)--at the cost of 300 thousand US dollars. The system has helped eliminate all possible human errors as seen in the open out cry trading procedures. Several international practices have been incorporated to make the system internationally compatible and modifications have also been made to customize the existing rules and regulations of the country.

2.1.9.2 Recruitment of new employees

In an effort to make the organization more efficient, NEPSE recruited 14 new employees for different positions under the open recruitment system on 2 September 2007. After a brief orientation six of them were placed in the Surveillance, Listing and Finance Departments and eight in the Trading and Human Resources Management Departments. In order to make its core business more efficient and smooth NEPSE has reformed its organization, introduced a new organizational chart and a Voluntary Retirement Scheme (45 per cent staffers opted for the scheme). Similarly, it also started outsourcing its non–core business, like security and cleaning services.

2.1.9.3 Trading through WAN started

After the introduction of the ATS and with the initiative and guidance of NEPSE, member brokers of NEPSE have started online trading through Wide Area Network (WAN) from their own office from 13 October 2007. Because of this facility, stock brokers can now sell or buy shares from their office. The brokers who have the necessary infrastructure prescribed by NEPSE will get access to WAN. To get access a broker must have a price board, separate rooms along with separate computers for clients' order entry, settlement and must provide up to date information to the clients. In the first phase, NEPSE granted permission to Malla and Mall Stock Broking Limited, Nepal Stock House, Nepal Investment and Securities Trading Private Limited, Shreekrishna Securities Limited and Premiere Securities Company Limited for trading through WAN. From the end of the FY 2007/08 all the 23 brokers transact from their office via WAN.

2.1.9.4 Market Halt System Introduced

NEPSE introduced a string of measure to stabilize the volatility of the stock market. Previously, NEPSE used to halt transactions of respective individual company by imposing the circuit breaker whenever share prices of the companies move up or down over 10 percent in a single day transaction.

As per new measure, it can also suspend the whole market trading, which is known as index based circuit breaker or market halt. Now on NEPSE can halt the trading floor for 15 minutes if the index moves up or down by three percent during the first half an hour. After resumption of trading if the index moves up or down by four percent, NEPSE can suspend trading for another half an hour. After the resumption if again the index changes by five percent, NEPSE can suspend trading for rest of the day. The new measure also require brokers to clearly list orders of buying and selling shares and place those orders

for transaction on priority basis. This provision has been enforced to address the rising concerns of small investors.

2.1.9.5 Trading Hours Extended

From 19 December 2007 NEPSE has increased the trading hours by one hour due to an increasing trading pressure after the automation of trading. Initially, NEPSE opened its trading activities for only two hours. Now the trading floor opens from 12.00 noon to 15.00.   NEPSE has expected that investors in general and small investors in particular will benefit from the increase in trading hours.

2.1.9.6 Real Time Information Disseminated

NEPSE has started providing real time information (live trading activity) to investors from 28 November 2008. Due to this facility investors can check share prices online from anywhere live during the trading hours. Additionally, without any time gap investors can check trading activities like top-gainers, top-losers, imposition of trading halt and resumption on NEPSE's web page.

2.1.9.7 Trading of Promoters' Shares

NEPSE began trading of promoters' shares on 31 March 2008, adopting a different price quoting mechanism for the first trading of promoters' shares of the listed companies. For the first trading, the price of the promoters' share of a company that has a positive net worth could not be less than five times of its net worth per share or half of the current market price of the ordinary share, whichever is low. Similarly, in the case of a company that has a negative net worth, the first trading price couldn't be below half of the current market price of the ordinary share. Earlier, one could have traded the promoters' shares on the basis of the market price of the ordinary share. It is expected that trading of promoters' shares will make the capital market more vibrant and stabilizes the prices of ordinary shares.

2.1.9.8 Publication of Newsletter, Monthly Market Statistics and Review

In its bid to make investors more aware of the secondary market NEPSE launched an English language newsletter, called 'NEPSE Newsletter', on 20 March 2008. Published once every two months, the newsletter will provide information on capital market activities. The newsletter will help reduce uncertainty and provide greater market efficiency through the dissemination of relevant information to investors and other concerned agencies and persons. NEPSE has also started publishing Monthly Market Statistics and Review from April 2008. It covers the secondary market related activities on a monthly basis.

2.1.9.9 OTC Market Started

NEPSE started the over-the-counter (OTC) market from 4 June 2008 to give shareholders a chance to sell or buy the shares of companies that are de-listed and that are not listed on NEPSE for failing to meet the listing criteria. The shares of 43 companies can now be traded in the OTC market. But as per the request of Nepal Rastra Bank NEPSE has decided to restrict the shares trading of Nepal Bank Limited in the OTC, since shares trading of Nepal Bank Limited will have a negative impact on the ongoing Financial Sector Reform Project.

2.1.9.10 NEPSE Converted to Profit Seeking Entity

The 26th annual general meeting (AGM) of NEPSE held on 23 May 2008 has decided to convert the organization into a profit seeking entity. The Company Registrar Office approved the decisions made at the AGM. The approval allowed NEPSE to turn itself into a profit seeking company, change its board of directors and increase its capital. Accordingly, NEPSE's authorized capital increased to Rs 160 million from Rs 50 million. Likewise, the paid-up capital was raised to Rs 50 million from the present Rs 34.9 million. Similarly, the structure of NEPSE's board was made more professional and representation having conflict of interest has been removed from the board.

2.2 Review of SEBON Regulations

The Securities Board of Nepal has made following provisions regarding the issuance of securities;

Public Issuance of Securities

a. If a Corporate Body intends to sale and distribute its securities to more than fifty persons at a time, it shall be required to make public issuance of securities. While selling securities through public offering the Corporate Body shall be required to set aside at least thirty percent of its issued for public subscription.

b. The corporate body making public issue pursuant to Sub-regulation (1) shall be required to have completed a minimum of one year of business operation under it objectives and also require to have already published the audited financial reports for the period.

c. The application for publicly issued shares pursuant to Sub-regulation (1) shall have citizenship certificate verified by the applicant attached thereto and also shall have to mention the name, address of the bank or financial institution where the applicant has maintained account and account number and the Issue Manager require to have arranged the refund of application money to be deposited in the bank account. Provided, however, that applicants subscribing for more than Rs. 50,000 require depositing the application money compulsorily through account payee check.

d. In case the application money so received has been deposited with the Banker to the Issue for interest, eighty percent of the interest so received shall be required to be given to the applicant in a proportion al basis for the days from the application date to the day before the allotment date and the Board shall be informed of such arrangement.

e. The body corporate while making public issue of securities pursuant to these regulations may reserve up to five percent of the share to the

working staffs and up to five percent for the local residents depending on the nature of business like hydropower, production or processing, out of the shares set aside for public issue. However, the shares reserves as such shall not be eligible to be sold or transferred within a minimum period of three years from the date of allotment.

f. Other provision related to the public issuance shall be prescribed by the Board under its directives.

g. In case a body corporate has issued securities without making public issue as prescribed by these regulations such securities shall not be eligible for trading through the stock exchange or an alternative trading system.

h. The Issue Manager shall be required to cancel any authorized application that it detects to have stated false information thereon. In case the Board finds that such application is not cancelled and the securities are distributed, the Board may impose fine equivalent to the same amount on the Issue and Sales Manager. The Board is required to use the proceeds only for the development of capital market.

2.3 Review of Journals and Articles

Aly, Mehdian & Perry (2007), in their article, *"An Analysis of Day-of-the-Week Effects in the Egyptian Stock Market",* have examined daily returns for the CMA Index from 2002-2006 to test for the Monday effect in the Egyptian equity market. The Egyptian stock market provides a unique opportunity to test for seasonal anomalies in an emerging and recently modernized stock exchange where trading takes place on a four-day week basis (Monday through Thursday) as opposed to the more traditional five-day week. The empirical results indicate that while Monday stock returns are significantly positive, they are not significantly different from returns during the rest of the week. Furthermore, Monday returns are significantly more volatile than returns from Tuesday to Thursday. Hence, the significantly positive returns on Monday are associated with returns that are more risky.

In addition, an intra-month return analysis provides evidence to indicate that the significantly positive Monday returns are not caused by higher returns during the last two weeks of the month. The overall implication of this study suggests that the emerging Egyptian market is at least weakly efficient. Therefore, no specific trading rule can be exploited to generate abnormal stock returns in the Egyptian stock market. Finally, it is important to note that Egypt, like other emerging equity markets has an immature capital market. Thus, the results presented here should be interpreted cautiously since the Egyptian stock market has a limited number (about 100) of stocks that are actively traded among the 1,071 listed stocks.

Cornell & Rutten (2008), in their article, *"Market Efficiency, Crashes, and Securities Litigation",* have stated that unless markets are fully efficient, which is not logically possible, estimates of damages based on the efficient market hypothesis and *ex post* analyses of stock price movements frequently will overstate damages, often significantly. The reason for the overstatement is that lawsuits are only filed in situations where large stock price declines have already been observed, and in such situations, the impact of even small inefficiencies typically will be exaggerated. A further reason is that the very possibility that a lawsuit may be filed may exacerbate the decline.

The foregoing demonstrates that even when the market is deemed efficient for purposes of showing reliance, it should not automatically be deemed efficient for purposes of estimating damages. This does not mean, however, that stock price data should no longer be used as a tool for estimating damages; the point is that it should be only one of many tools. Stock price data by itself cannot answer whether the price decline is commensurate with the fundamental news conveyed by a fraud-related disclosure and thus whether the drop is a meaningful estimate of actual damages. Other standard valuation techniques, such as discounted-cash-flow analyses, must be brought back into securities litigation to answer that crucial question. Fortunately, standard valuation

models and analyses of stock price movements focus on varying aspects of the problem of estimating damages, such that any errors, oversights, or elements of speculation involved in the application of one approach typically will differ from those that are likely to arise when applying the other. Consequently, using both techniques in conjunction with each other, and comparing the results, will give a more balanced and accurate measure of true damages than either applied alone.

Tetlock (2009), in his article, *"Does Liquidity Affect Securities Market Efficiency?"* has stated that it is challenging to estimate the relationship between liquidity and market efficiency using data from conventional financial markets, where securities' fundamentals cannot be observed and systematic risks affect pricing. Securities markets with persistently high liquidity show significant pricing anomalies, such as overpricing low probability events and under pricing high probability events. Conversely, the sporadically liquid and illiquid securities markets are remarkably efficient. A leading explanation is that illiquid markets have fewer noise traders, and periods of illiquidity prevent arbitrageurs from profiting on short-term trades that would destabilize prices.

Further liquidity serves as a proxy for non-informational or noise trading. The key finding is that the prices of illiquid securities converge toward terminal cash flows much more rapidly than the prices of liquid securities. This implies that non-informational or noise trading is prevalent during periods of liquidity, which may help explain the observed mispricing in liquid securities. Although these results are unlikely to generalize without modification to conventional financial markets with long-horizon securities and larger stakes, they do suggest three interesting directions for future research. First, liquidity may only appear to be a priced risk factor because it captures some systematic element of mispricing. Second, different types and sources of liquidity may have opposing effects on the costs of arbitrage and equilibrium mispricing—*e.g.*, liquidity from noise trading may harm efficiency, whereas liquidity from low search

costs may enhance efficiency. Third, because there appear to be significant limits to arbitrage on an online exchange with few capital constraints and securities that expire within a single day, the limits to arbitrage in conventional markets may be more severe than previously thought.

McKinley (2010), in his article, *"Stock Market Efficiency and Insider Trading"* has stated that insiders could significantly outperform the market by either buying or selling shares of their company's stock in both the short and long term. However, after statistical analysis was performed on the data it became apparent that insider trading was not so profitable. The data suggest that no form of insider trading, buying or selling, is profitable in the short run (one to six months). After performing statistical analysis, it has been concluded that it takes about one year for insider information to become public and reflected in a stock's price.

However, not all insider trading is profitable in the long run. Stocks that were sold by insiders under-perform the market after one year. The one-year data for insider buying proved to be statistically insignificant. The inability of insiders to profit from purchasing shares in their own company may be due to their lack of knowledge about competitors coupled with overconfidence in their ability to manage their company.

Caccese (2010), in her article, *"Does Noise Trading Affect Securities Market Efficiency?"* has stated that securities markets with more noise traders show significant pricing anomalies, such as overpricing low probability events and under pricing high probability events. Conversely, the securities markets where few noise traders are present appear to be remarkably efficient. Even more remarkable, only the highly liquid markets with persistent noise trade exhibit the S-shaped pattern of mispricing. Prices in securities markets in which noise trade is high at the moment, but could dissipate in the future, are reasonably accurate forecasts of empirically observed event frequencies.

As a result of limited arbitrage, small unexploited arbitrage opportunities remain in equilibrium. However, competition among arbitrageurs appears sufficient to prevent the equilibrium trading profits from becoming excessive. Although these results are unlikely to generalize without modification to real world financial markets with long-horizon securities, they do suggest three interesting directions for future research. First, liquidity may appear to be a priced risk factor because it captures some systematic element of mispricing. Second, future theoretical models could distinguish between persistent liquidity and sporadic liquidity. Third, because there appear to be significant limits to arbitrage on an online exchange with few capital constraints and securities that expire within a single day, the limits to arbitrage on real-world exchanges may be more severe than previously thought.

2.4 Review of Thesis

Shakya (2007), in his thesis, *"Role of Financial Indicators in Determining Share Price in Nepalese Financial Market",* has the main objective to measure the role of stock price determinants. The other specific objectives are:

  a. To examine and evaluate the relationship of MPS with various financial indicators like NWPS, EPS, DPS, ROE, etc.
  b. To analyze the market trends of MPS with various financial indicators like EPS, NWPS, DPS, ROE, etc.
  c. To find out whether stocks of the sampled companies are equilibrium priced of not.
  d. To identify qualitative factors affecting the stock price.

The major findings of the study are;

  a. NABIL's MPS is positively correlated with all financial indicators but these values are not statistically significant at either 5% or 10% level of significance.
  b. NIBL's MPS has negative correlation with all financial indicators.

c. For all other banks, the correlation coefficients of MPS with other financial indicators are both positive and negative. These values are statistically significant at either 5% or 10% level of significance.

d. Relationship with all financial indicators of MPS for NFCL is positively correlated and the relationship is statistically significant at 5% level of confidence with EPS and at 10% level of confidence with NWPS and DPS.

e. For other Finance Companies, the correlation coefficient of MPS with other financial indicators, are both positively and negatively correlated and the relationship is statistically significant for KFL and UFCML and for others it is insignificant.

Satyal (2008), in his thesis, *"Stock Price Determinants in Nepal Stock Exchange"*, has a major objective of identifying the prime determining factor of share price fluctuation of Nepalese Commercial Banks. The other supporting objectives of his research are:

a. To examine and evaluate the relationship between MPS with the various financial indicators like EPS, BPS, DPS etc.

b. To analyze the market trends of MPS with financial indicators.

c. To conduct the opinion survey of potential investors regarding various aspects of share behaviours in Nepal.

The major findings of the study are:

a. DPS of BOK is much volatile in comparison to MPS, BPS and EPS. Bank of Kathmandu has positive correlation with between their Market price per share and DPS, BPS and EPS. This indicates that they directly affect the Share Price of BOK.

b. BPS and EPS are positively correlated in the case of Everest Bank Limited whereas DPS is negatively correlated. This indicates that increase in DPS of this Bank don't contribute on the increase of Share Price rather it decreases it. But increase in BPS and EPS increase the

share price and vice versa. DPS is much volatile in comparison with MPS, BPS and EPS.

c. The correlation between MPS and other indicators are found to be insignificant for most of Banks. It shows that they individually influence very less but jointly they influence a lot. There can be other factors which influence the share price of the organisation.

d. Dividend pattern plays a great role on share price movement. Higher the DPS, more will be the Share Price. Most of the investors like to analyse the Dividend pattern of the company before they invest in their shares.

Burlakoti (2009), in his thesis, *"Stock Price Behaviour of Financial Institutions and Commercial Banks",* has the main objective to analyze the stock price behaviour. The other specific objectives of the study are;

a. To study the present position of the financial institution and joint venture banks.

b. To examine and evaluate the relationship of MPS with various financial indicators like EPS, NWPS, DPS and DPR.

c. To analyze the degree of risk involved in the common stocks investment of the sampled companies.

d. To identify whether stocks of the sampled companies equilibrium priced or not.

e. To analyze and have the comparative study about the performance of financial institution and commercial banks with regard to their profitability and liquidity position.

f. To present some recommendations based on the findings of the study.

The major findings of the study are;

a. The DPS of SCBL has higher than NBL, NIBL and EBL. In finance companies, DPS of NFCL is higher than AFCL, NMBCL. It is seen that DPS of NFCL is in satisfactory level.

b. The MPS of SCBL is higher than NBL, NIBL and EBL. SCBL is the most appreciable bank among the selected ones. The risk of NBL is higher than SCBL, NIBL and EBL. It indicates that there is high risk in NBL. The CV of EBL is more fluctuating i.e. there is higher CV in EBL.

c. The correlation coefficient of EPS and DPS seems to be significant except the case of EBL and AFCL, i.e. correlation coefficient recorded as EBL & AFCL is in negative.

d. In case of NIBL & NFCL there exists negative correlation coefficient of EPS & NWPS which is insignificant which shows that there is higher degree of managerial problem in issuing and managing shares of NIBL & NFCL.

e. The coefficient of determination (r^2) of SCBL, NIBL, NFCL & NMBFCL are strong of 0.64, 0.254, 0.7174, 0.393 which indicates that 64%, 25.4%, 71.74% & 39.3% of the total variation in market price has been explained by the influence of EPS and remaining 36%, 74.6%, 28.26%, 60.7% is due to the effect of other factors.

Rayamajhi (2010), in her thesis, *"Share Price Behaviour of Commercial Banks listed in NEPSE",* has a major objective to analyse the behaviour of share price. The specific objectives of the study are:

a. To analyze the stock price movement of the NEPSE market.

b. To test the random walk or weak efficient market hypothesis.

c. To test whether the successive price changes are independent or dependent with the price of historical change.

The major findings of the study are:

a. The total numbers of actual and expected runs are statistically significant for most of the equity shares, which implies that their price changes are significantly different from random series. Result of run test also supports the result of autocorrelation. Therefore, today's price change is dependent on the information of yesterday's price.

b. The mean absolute values of the autocorrelation coefficients are lower when the lag days are increases. This means the information of past price changes have little role to predict the future price changes for longer days.

c. Half of the sample companies' share have greater than average value of K (18.87%) difference between actual and expected number of runs, which indicates significant difference between the actual and expected number of runs.

d. Because the persistence hypothesis has been supported by the result of autocorrelation and run test, professional investors either individual or institutional can beat the market. Therefore, to make greater profit than "naïve buy and hold strategy", acute fundamental or other analysis are required which accurately predict the appearance of the new information in the market that affects the price of shares.

e. There exists a low order serial dependence, which helps in certain extent to increase investor's expected profit.

2.5 Research Gap

All of the above reviewed studies are concentrated on measuring the behavior of share price, which is just the ramification of the securities. Thus, considering this deficiency, the present study has been conducted to analyze the securities market of Nepal, the problems, prospect, and malpractices of the securities market. In addition, the study also analyzes the contribution of the market capitalization in gross domestic product and analyzes the composition of turnover of Nepal Stock Exchange.

CHAPTER - III
RESEARCH METHODOLOGY

3.1 Research Design

The study basically analyses the trend and performance of NEPSE based on macro picture along with future predictions. To have an in-depth enquiry, the securities performance of NEPSE is analyzed. The data for the study is collected from both secondary and primary sources and the collected data is presented and analyzed using different tables, figures and statistical tools. Thus presentation and analysis are the core aspects of this study. In this perspective, this research follows descriptive and exploratory research design.

3.3 Population and Sample

NEPSE is involved in securities transactions in country. For the study all the listed companies have been assumed to be the population. To elaborate the securities market of the country, the analysis of the performance of NEPSE is crucial, thus the performance of the NEPSE as a whole has been considered as both population and sample.

3.3 Nature and Sources of Data

Both secondary and primary sources of data have been quested for the collection of data. The secondary data have been collected mainly through the annual and trading reports of NEPSE, the annual reports of SEBON and the reports of Central Bureau of Statistics. Further, the official websites of these institutions along with that of National Planning Commission have been visited. However, the primary data have been collected through opinion survey.

3.4 Data Analysis Tools

For the analysis of the data, both financial and statistical tools have been extensively used.

3.4.1 Financial Tools

The major financial tools used in the study are as follows;

a) Trend Analysis of NEPSE Index

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

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

$$P_{01} \ X \frac{P_1 x Q_1}{P_0 x Q_0} \ x100$$

Where,

P_{01} = NEPSE Price Index

P_1 = Today's Stock Price

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

Q_0 = Base Listed Shares.

b) Company Trading Ratio

The company trading ratio is the ratio of the number of traded companies to the total number of listed companies. It is not necessary that the shares of all the companies listed in the stock exchange are traded, so the listed companies whose shares are traded in the stock exchange are called traded companies. The company trading ratio measures the liquidity of a stock exchange i.e. higher the company trading ratio higher the liquidity and vice-versa. The company traded ratio can be calculated as;

$$\text{Company Trading Ratio} = \frac{\text{Number of Traded Companies}}{\text{Number of Listed Companies}}$$

c) Market Capitalization Ratio

The market capitalization ratio is the ratio of market capitalization to the nominal Gross Domestic Product (GDP). The market capitalization ratio can be used as a measure of market size. This ratio serves as an indicator of stock market development under the assumption that stock market size is positively correlated with the ability to mobilize capital and diversify risk. Generally, the market capitalization of developed stock market is greater than 1. The market capitalization ratio is calculated as;

$$Market\ Capitalization\ Ratio = \frac{Market\ Capitalization}{GDP\ at\ Producers'Price}$$

d) Value Traded Ratio

The value traded ratio is the ratio of total amount traded on the stock market to the nominal Gross Domestic Product (GDP). It measures the organized trading of firm equity as a share of national output. While not a direct measure of trading costs or the uncertainty associated with trading on a particular market, the assumption behind the value traded ratio is that it positively reflects liquidity on an economy-wide basis. The value traded ratio is the complementary of the market capitalization ratio. Thus, for the measurement of liquidity of a market, both the ratios; market capitalization ratio and value traded ratio are required to get the fact. For the developed market, the value traded ratio is greater than 0.4. The value traded ratio can be calculated as;

$$Value\ Traded\ Ratio = \frac{Value\ Traded}{GDP\ at\ Producers'Price}$$

e) Stock Turnover to Market Capitalization Ratio

It is the ratio of turnover to the market capitalization. Though, it is not direct measure of theoretical defilation of liquidity, high turnover is often used as indicator of low transaction cost. The turnover ratio complements market capitalization ratio. A large but inactive market can have a large market capitalization ratio but a small turnover ratio. While the value traded ratio captures trading relative to the size of stock market. A small liquid market can

have a high turnover ratio but a small value traded ratio. The turnover ratio can be calculated as;

$$\text{Stock Turnover to Market Capitalization Ratio} = \frac{\text{Stock Turnover}}{\text{Market Capitalization}}$$

3.4.2 Statistical Tools

The major statistical tools used in the study are as follows:

A) Mean

The arithmetic <u>mean</u> (or simply the mean) of a list of numbers is the sum of the list divided by the number of items in the list. The mean is the most commonly-used type of <u>average</u> and is often referred to simply as the average.

$$\text{Mean}(\bar{X}) = \frac{x_1 + x_2 + \ldots \ldots \ldots + x_n}{N}$$

B) Standard Deviation

Standard deviation is a widely used measure of the variability or <u>dispersion</u>, being algebraically more tractable though practically less <u>robust</u> than the <u>expected deviation</u> or <u>average absolute deviation</u>. It may be thought of as the average difference of the scores from the mean of distribution, how far they are away from the mean. A low standard deviation indicates that the data points tend to be very close to the <u>mean</u>, whereas high standard deviation indicates that the data are spread out over a large range of values.

$$\text{Standard Deviation }(\sigma) = \sqrt{\frac{\Sigma(X - \bar{X})^2}{N}}$$

C) Coefficient of Variation

The coefficient of variation represents the ratio of the standard deviation to the mean, and it is a useful statistic for comparing the degree of variation from one data series to another, even if the means are drastically different from each other.

$$C.V. = \frac{\text{Standard Deviation} \times 100}{\text{Mean}}$$

D) Regression

Regression refers to any approach to modeling the relationship between one or more variables denoted Y and one or more variables denoted X, such that the model depends linearly on the unknown parameters to be estimated from the data. The simple regression line of Y on X is given by;

$$Y = a + bX \dots\dots\dots\dots\dots\dots\dots\dots \text{ (i)}$$

Where, Y = Dependent Variable

    a = Constant

    b = Regression Coefficient

    X = Independent Variable

E) Trend Analysis

Trend analysis is an analysis of financial ratio over time used to determine the improvement of deterioration of financial situation. Using the least square method, the projection for two years is done. For the estimation of linear trend line, following formula has been used.

$$Y = a + bx$$

Where,

    Y = dependent variable

    a = y-intercept

    b = slope of the trend line

    x = independent variable

CHAPTER – IV

DATA PRESENTATION AND ANALYSIS

4.1 Secondary Data Analysis

This section of the study is mainly concentrated to analyze the secondary data collected and thus this section attempts to fulfill the first three objectives of the study set out in the first chapter, which includes analyzing the trend of securities, assessing the financial perspective of securities and estimating the index and others in the future.

4.1.1 Analysis of Securities System in NEPSE

Nepal Stock Exchange had opened its trading floor on 13th January, 1994. From that time, NEPSE is involved in the securities trading of different listed companies. Here, attempts have been made to study the status of NEPSE by analyzing its yearly trends on different factors for five fiscal i.e. from FY 2004/05 to FY 2008/09.

4.1.1.1 NEPSE Index

In course of transactions, the price of some companies' stock would increase while the price of other companies' stock may decline over time. However, if the overall performance of the stock market has to be analyzed, an index is needed. Market index serves this purpose. Market index can be computed by using different techniques. However, NEPSE uses value weighted index technique. For the computation of value weighted index, NEPSE has assumed 30 Magh, 2050 (12th Feb, 1994) as base period.

Table 4.1

Closing NEPSE Index

Fiscal Year	Closing NEPSE Index	Percentage Change
2004/05	286.67	29.11
2005/06	386.83	34.94
2006/07	683.95	76.81
2007/08	963.36	40.85
2008/09	749.10	-22.24

(Source: Trading Reports, NEPSE)

The table manifests that NEPSE index is 286.67 points at the beginning of the fiscal year 2004/05 and it is 749.10 points in the fiscal year 2008/09. The NEPSE index has increased highest (76.81%) in the fiscal year 2006/07 and finally decreased by 22.24% in the fiscal year 2008/09 compared to the index of previous year. As per the annual report of NEPSE, the NEPSE index reached the high of 1175.38 on 31st August 2008 and the low of 609.46 on 22nd January 2009 in the fiscal year 2008/09. Moreover, the sub-index of listed hydropower is greatest in the fiscal year 2008/09. The sub-index of hydropower is points, commercial banks is 780.87, manufacturing and processing is 434.32 points, hotel is 367.42 points, trading is 295.83 points, insurance is 656.41 points, finance is 697.61 points, development bank is 772.56 points and other is 738.99 points at the end of the fiscal year 2008/09. The instability of the government, strike, malpractices in the stock market, investors enthusiasm to other sectors like real estate and others have greatly influenced the securities market of Nepal in the fiscal year 2008/09, as a result the NEPSE index has been caused to decline in comparison to that in the fiscal year 2007/08.

Figure 4.1

NEPSE Index
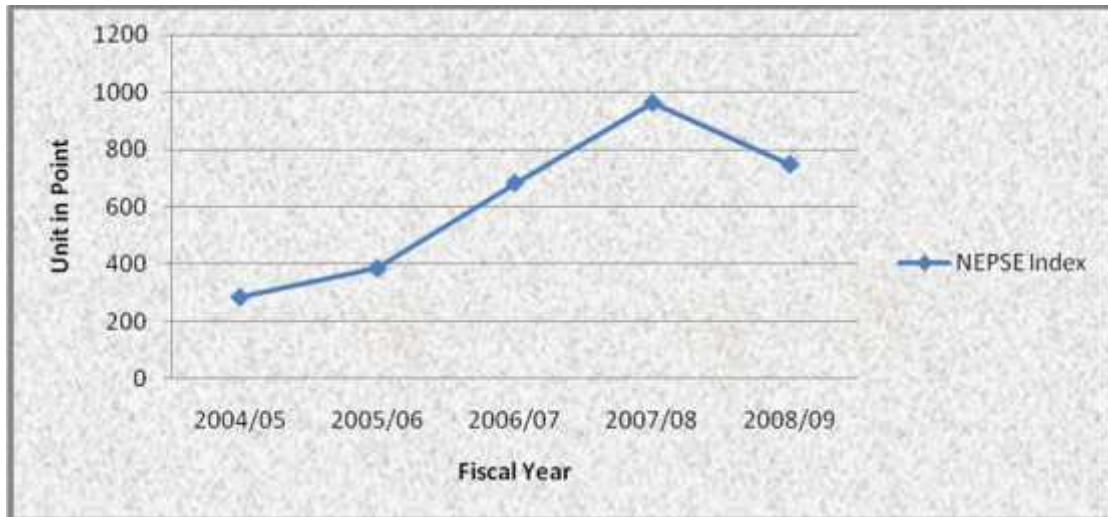
4.1.1.2 Turnover of NEPSE

Under this section the turnover generated by NEPSE through the transaction of securities, including both share and bond transactions, is elaborated and the growth rate in total turnover has been highlighted.

Table 4.2

Annual Turnover of NEPSE

Fiscal Year	No. of Shares (000)	Share Turnover (million)	No. of Bonds (000)	Bond Turnover (Million)	Total Turnover (Million)	Growth Rate (%)
2004/05	18433.55	4507.68	1500	150	4657.68	117.22
2005/06	12221.93	3451.43	38660	4910	8361.43	79.52
2006/07	18147.25	8360.10	33650	3950	12310.10	47.22
2007/08	28599.77	22820.76	62725	7825	30645.76	148.95
2008/09	30547.16	21681.14	156835	20485	42166.14	37.59
Average		**12164.22**		**7464.00**	**19628.22**	
S.D.		**8404.05**		**6957.62**	**14380.24**	
C.V. %		**69.09**		**93.22**	**73.26**	

(Source: Annual Reports, NEPSE)

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The table manifests the annual turnover of the NEPSE rendered through the trade of the shares and the bond. The turnover of the NEPSE is highly outweighed by the shares business. The number of shares transacted has decreased in the fiscal year 2005/06, and then it has followed increasing trend and thus finally reached to 30547.16 thousands in the fiscal year 2008/09 from 18433.55 thousands in the fiscal year 2004/05. However, the turnover of shares transactions could not remain highest, alike the number of shares, in the fiscal year 2008/09. The highest turnover through shares transactions is in the fiscal year 2007/08, which is precisely Rs. 22820.76 millions, and in the fiscal year 2008/09 it is Rs. 21681.14 millions. Within the five fiscal years, the stock exchange has accumulated Rs. 12164.22 millions turnover per year with the high variations of 69.09%.

Moreover, the stock exchange has started bond market business from the fiscal year 2004/05, and at initial, it has transacted 1500 thousands government bond with the paid up value of Rs. 150 millions. Then from the fiscal year 2005/06, NEPSE has transacted both government bond and corporate bond and at the end of the fiscal year 2008/09, NEPSE has transacted 151500 thousand government bond and 5335 thousand corporate bond. In total, the number of bond transactions has ranged from 1500 thousand in the fiscal year 2004/05 to 156835 thousand in the fiscal year 2008/09, and the turnover from bond transactions has ranged from Rs. 150 millions in the fiscal year 2004/05 to Rs. 20485 millions in the fiscal year 2008/09. In average, the bond transaction per year worth Rs. 7464 millions with the variation of 93.22%.

Further, the total turnover, share and bond transactions, of NEPSE has consistently followed increasing trend in the observed periods. The turnover of the NEPSE is Rs. 4657.68 millions in the fiscal year 2004/05 and Rs. 42166.14 millions in the fiscal year 2008/09. Likewise, the average turnover of the stock exchange is Rs. 19628.22 million with the variation of 73.26%. Though the turnover has increased in each year, the growth rate in turnover has been

ascertained to be greatest, 148.95%, in the fiscal year 2007/08. In overall, it can be assumed that the charm of the securities market in investors have been growing in greater extent and thus investors are defraying more market price for taking the possession on shares.

Figure 4.2

Annual Turnover of NEPSE
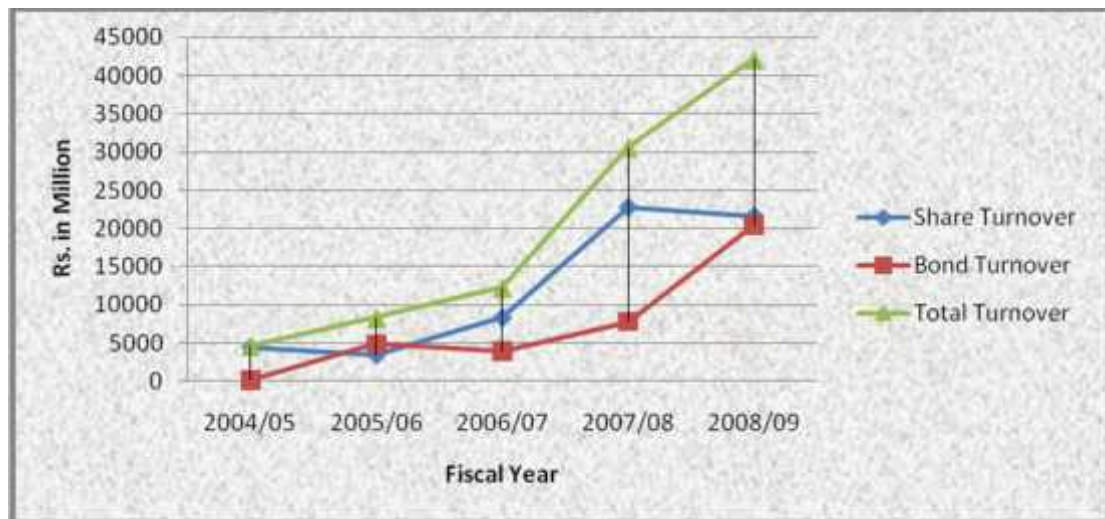
4.1.1.3 Market Capitalization of NEPSE

This indicates the total market value of the listed companies during the study period. The total market capitalization of listed companies and the percentage change in the five year period is presented in the Table 4.3.

Table 4.3

Annual Market Capitalization

Fiscal Year	Market Capitalization (Rs. in million)	Growth Rate (%)
2004/05	61365.89	48.14
2005/06	96763.74	57.68
2006/07	186301.28	92.53
2007/08	366247.56	96.59
2008/09	512939.07	40.05

(Source: Trading Reports, NEPSE)

The above table shows that the market capitalization of the listed companies has followed increasing trend. The market capitalization has ranged from Rs.

61365.89 millions in the fiscal year 2004/05 to Rs. 512939.07 millions in the fiscal year 2008/09. The growth rate in market capitalization is highest (96.59%) in the fiscal year 2007/08 and lowest (40.05%) in the fiscal year 2008/09. The increasing trend of market capitalization indicates increase in market price per share of the companies listed, which indicates positive impact of securities market on the investors.

Figure 4.3

Market Capitalization of NEPSE
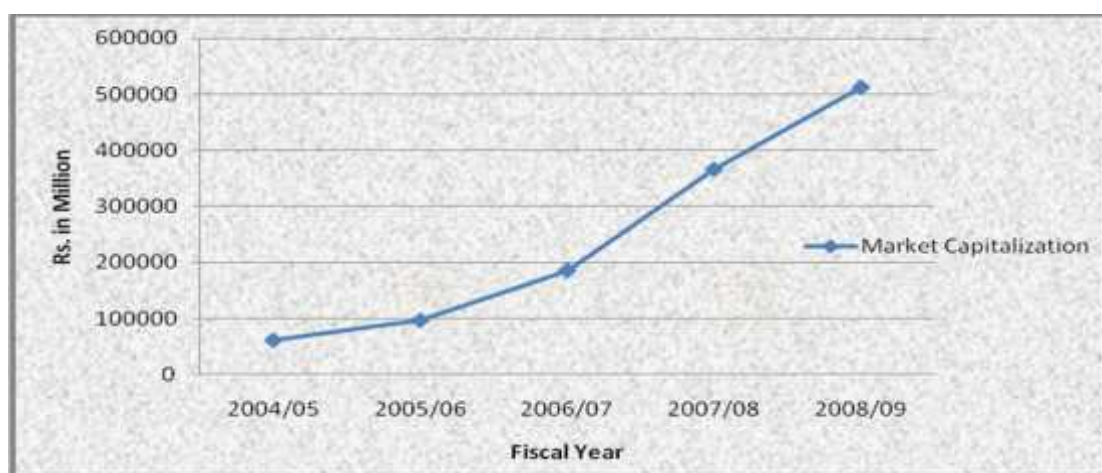
4.1.1.4 Listed and De-Listed Companies in NEPSE

As per the rules and regulations of SEBON, the company should be listed on the NEPSE to transact shares in market. The number of companies listed indicates the increasing/decreasing trend of the number of companies listed per year and de-listed companies indicates that the companies have not acted as per the provision of SEBON. The number of companies listed and its growth along with the number of de-listed companies are presented in the table.

Table 4.4

Listed and De-Listed Companies in NEPSE

Fiscal Year	Listed Companies	Growth %	De-Listed
2004/05	125	9.65	0
2005/06	135	8.00	0
2006/07	135	0.00	12

|			
2007/08	142	5.19	5
2008/09	149	4.93	0

In the fiscal year 2006/07, the stock exchange de-listed 12 companies for non-compliance of legal provisions. Out of 150 listed companies with the listing of 13 new companies with the merging of NB Finance and Leasing Company with the NB Bank and de-listing of five companies, the total number of listed companies remained to be 142 during the fiscal year 2007/08. De-listed companies have been either already closed or have not held annual general meetings or have not audited their results for more than two years. Altogether shares amounting Rs. 348.20 and Rs. 174.91 million have been de-listed during the year fiscal year 2006/07 and 2007/08.

After adjusting the delisted companies, the number of listed companies in NEPSE has followed increasing trend in each fiscal year. However, in the fiscal year 2006/07, the number of listed companies has remained uniform compared to that of the fiscal year 2005/06. At the end of the fiscal year 2008/09, the number of listed companies has counted to 149. The increasing trend of listed companies indicates good prospect of securities transactions. The growth of listed companies has almost been in decreasing trend though not negative. This indicates that the NEPSE might have incorporated most of the institutions and thus there is slow growth in listing. The listed companies have flourished highest by 9.65% in the fiscal year 2004/05.

Figure 4.4

Listed and De-Listed Companies in NEPSE
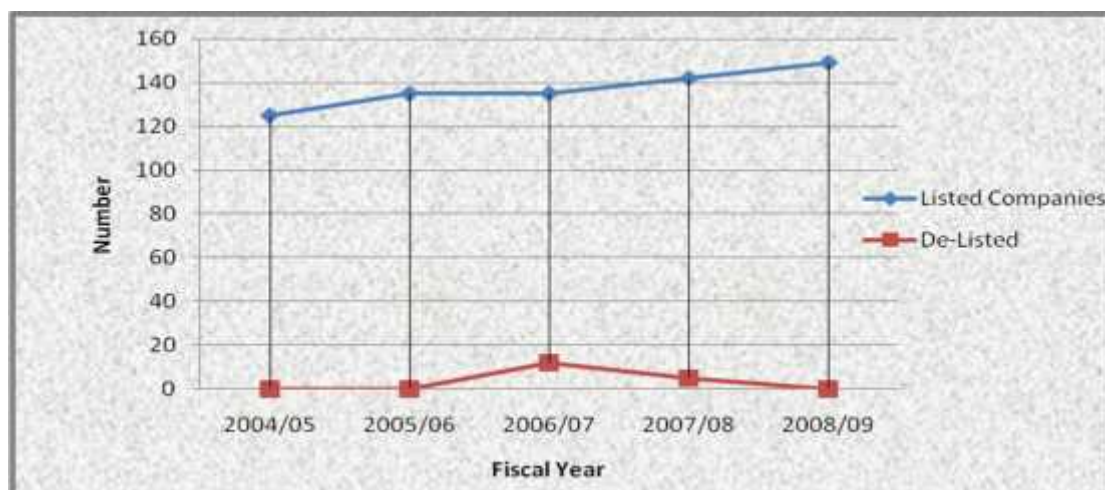
4.1.2 Financial Perspective of Securities Trading System

Liquidity is another aspect that is facilitated by the stock exchanges. Liquid equity market provides investment opportunities to the investors and to make a certain assets more attractive. It allows savers to acquire asset and sell it quickly and cheaply. Different ratios can be used to witness the liquidity of a stock market. Here Company Trading Ratio, Market Capitalization Ratio, Value Traded Ratio, and Turnover Ratio are employed to find out the liquidity position of NEPSE.

4.1.2.1 Company Trading Ratio

It is not necessary that the shares of all the companies listed in the stock exchange are traded, so the listed companies whose shares are traded in the stock exchange are called traded companies. The company trading ratio measures the liquidity of a stock exchange i.e. higher the company trading ratio higher the liquidity and vice-versa.

Table 4.5

Company Trading Ratio

Fiscal Year	Traded Company	Listed Company	CTR (%)
2004/05	102	125	81.60
2005/06	110	135	81.48
2006/07	116	135	85.93
2007/08	136	142	95.77

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2008/09	137	149	91.95
Mean	**120**	**137**	**87.35**
S.D.	**14.03**	**8.01**	**5.68**
C.V. %	**11.68**	**5.84**	**6.51**

Clearly, the number of traded companies has followed increasing trend in the five observed periods. The number has risen from 102 in the fiscal year 2004/05 to 137 in the fiscal year 2008/09. However, this increment has not cope with the increment in listed companies, as a result the ratio of number of traded companies to listed companies has fluctuated during the periods. The table depicts that in the fiscal year 2004/05, 81.60% of the companies listed in NEPSE have traded their securities. Likewise, the ratio has slightly decreased to 81.48% in the fiscal year 2005/06, and then it has increased to 85.93% in the fiscal year 2006/07, increased to 95.77% in the fiscal year 2007/08 and finally it has decreased to 91.95% in the fiscal year 2008/09. The ratio shows that the fiscal year 2007/08 has remained the most satisfactory as 95.77% of the companies listed have been traded. In average, only 87.35% of the listed companies in NEPSE have been traded within the five observed periods. NEPSE should monitor the obstacles in the market that are preventing the listed companies to remain untraded.

Figure 4.5

Company Trading Ratio
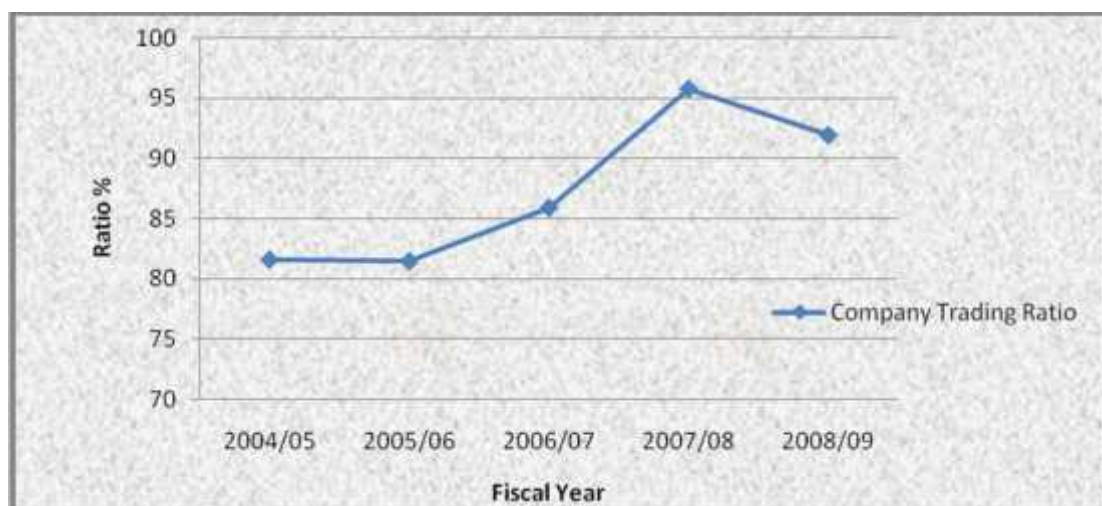
4.1.2.2 Market Capitalization Ratio

The market capitalization ratio is the ratio between market capitalization and Gross Domestic Product (GDP). Market Capitalization Ratio shows the contribution of market capitalization to the GDP. Market capitalization ratio of different fiscal years are calculated and presented in the table.

Table 4.6

Market Capitalization Ratio

Fiscal Year	Market Capitalization (Rs. in million)	GDP at Producer's Prices (Rs. in million)	Market Capitalization Ratio (%)
2004/05	61366.90	589412	10.41
2005/06	96763.70	654055	14.79
2006/07	186301.30	727089	25.62
2007/08	366247.56	820814	44.62
2008/09	512939.07	859392	59.69
Mean			**31.03**
S.D.			**18.57**
C.V.%			**59.84**

(Source: Central Bureau of Statistics and Annual Report 2008/09, NEPSE)

The market capitalization of securities has been ascertained to be in increasing trend. This indicates that the pace of growth in market capitalization is greater than the pace of growth in GDP at producer's price. The ratio of market capitalization to GDP is 10.41% in the fiscal year 2004/05, which has gradually increased in each fiscal year, and by the end of the fiscal year 2008/09, it is 59.69%. In average, the ratio of market capitalization to total GDP is 31.03%, which indicates that market capitalization has substantial role to stimulate the GDP growth. However, the ratio has highly varied in the five year periods,

since the coefficient of variation in the ratio is 59.84%. Nonetheless, it can be assumed that the development of securities market has crucial role to upgrade the GDP and thus buttress the economy of the country.

Figure 4.6

Market Capitalization Ratio
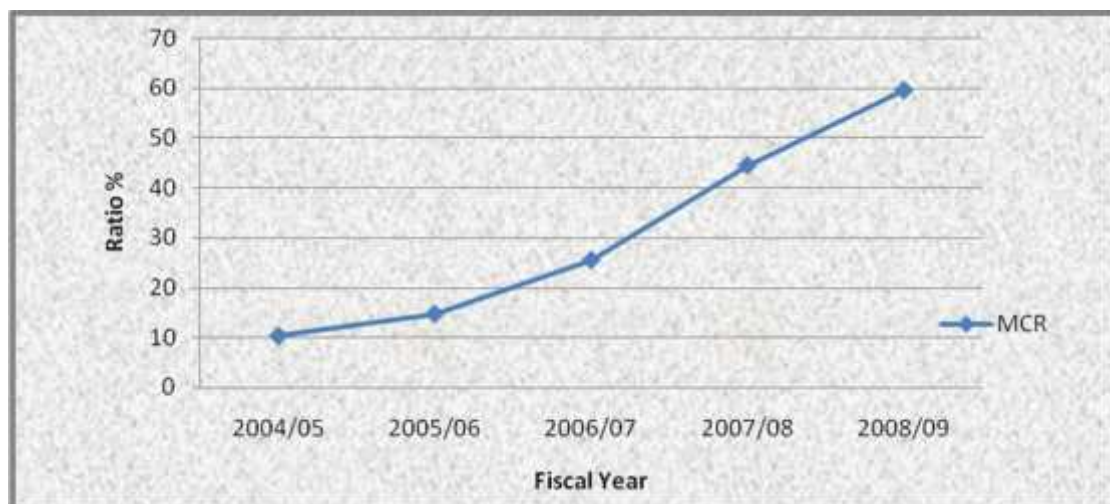
4.1.2.3 Value Traded Ratio

Value traded ratio is the complementary of the market capitalization ratio. The value traded ratio is the ratio of value traded or turnover to the Gross Domestic Product (GDP). For testing the liquidity of the security market, value traded ratio is also needed to compare.

Table 4.7

Value Traded Ratio

Fiscal Year	Stock Turnover	GDP at Producer's Prices	Value Traded Ratio (%)
2004/05	4507.68	589412	0.76
2005/06	3451.43	654055	0.53
2006/07	18147.25	727089	2.50
2007/08	22820.76	820814	2.78
2008/09	21681.14	859392	2.52
Mean			**1.82**
S.D.			**0.97**
C.V.%			**53.07**

(Source: Central Bureau of Statistics and Annual Report 2007/08, NEPSE)

It has been ascertained that the value traded ratio has oscillated during the observed periods. The ratio has decreased from 0.76% in the fiscal year 2004/05 to 0.0.53% in the fiscal year 2005/06 and then it has increased to 2.50% in the fiscal year 2006/07 and again it has increased to 2.78% in the fiscal year 2007/08 and finally decreased to 2.52% in the fiscal year 2008/09. However in average, the annual turnover has contributed 1.82% of the total GDP of the country. Thus for the economic prosperous of the country, the uplift in annual turnover of securities market is quite necessary.

Figure 4.7

Value Traded Ratio
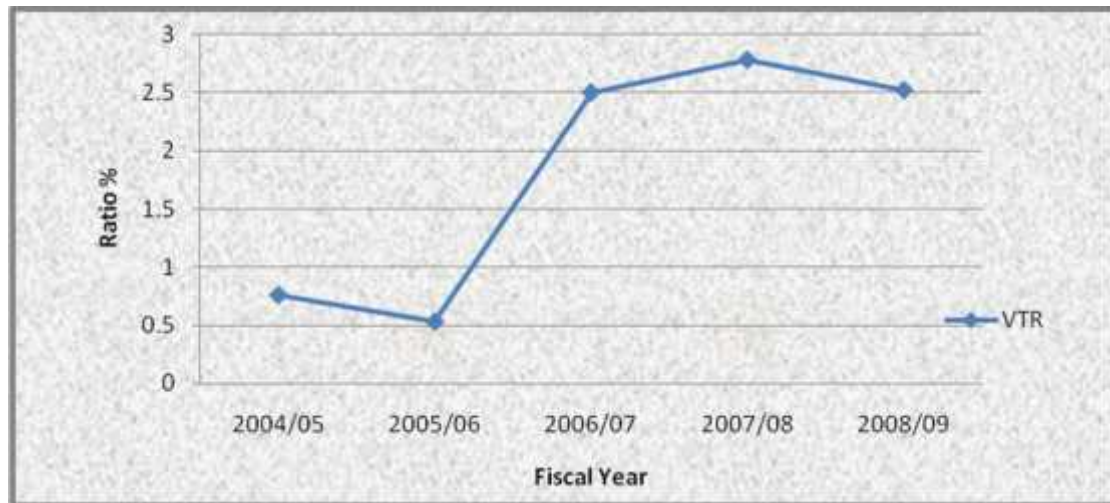
4.1.2.4 Stock Turnover to Market Capitalization Ratio

The turnover to market capitalization ratio calculates the activeness of the share market. This ratio calculates the trading relative to the size of the stock market. Turnover ratio is used to determine the liquidity of the stock market. Higher the turnover ratio, higher will be the liquidity and vice-versa. Turnover Ratios during different fiscal years from FY 2004/05 to FY 2008/09 are calculated and presented in the following table:

Table 4.8

Stock Turnover to Market Capitalization Ratio

Fiscal Year	Stock Turnover	Market Capitalization	STMCR (%)
2004/05	4507.68	61365.89	7.35
2005/06	3451.43	96763.74	3.57
2006/07	18147.25	186301.28	9.74
2007/08	22820.76	366247.56	6.23
2008/09	21681.14	512939.07	4.23
Mean			**6.22**
S.D.			**2.22**
C.V.			**35.70**

(Source: Annual Reports, NEPSE)

The turnover to market capitalization has oscillated during the observed periods. The table shows that the turnover to market capitalization of the listed companies has ranged from 3.57% in the fiscal year 2005/06 to 9.74% in the fiscal year 2006/07. The turnover to market capitalization has started from 7.35% in the fiscal year 2004/05, decreased to 3.57% in the fiscal year 2005/06 and then increased to 9.74% in the fiscal year 2006/07 and again decreased to 6.23% in the fiscal year 2007/08 and finally reached to 4.23% in the fiscal year 2008/09. However, NEPSE has utilized 6.22% of the market capitalization in average in generating turnover. The standard deviation and coefficient of variation of turnover to market capitalization are 2.22 and 35.70% respectively. The coefficient of variation has indicated that turnover to market capitalization of NEPSE fluctuated by 35.70% during the observed periods. It would be better if NEPSE follows the rules and regulations effectively to have high turnover ratio and thus to have satisfactory liquidity.

Figure 4.8

Stock Turnover to Market Capitalization Ratio
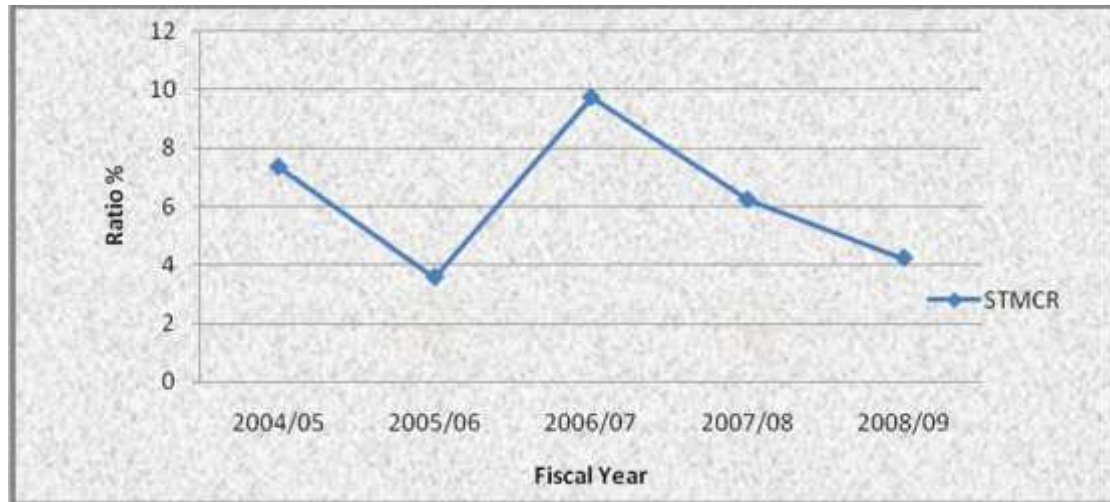
4.1.2.5 Analysis of Present Status

Present condition of NEPSE is expected to be better than the past but it can not be considered as a satisfying condition. To predict the condition of NEPSE in future, the analysis of present status is the most. For the analysis of current status of NEPSE, monthly analysis has been done in different aspects during the last FY 2008/09.

4.1.2.5.1 Number of Listed Companies under Different Sectors in FY 2008/09

The number of listed companies in NEPSE at the end of fiscal year 2008/09 was 149. These companies are categorized into 8 different sectors. Each sector possesses the different number of listed companies. The numbers of listed companies according to the sectors are presented in the table 4.9.

Table 4.9

Sector-wise Number of Listed Companies in FY 2008/09

Sectors	Numbers	Percentage
Commercial Bank	21	14.09
Development Bank	28	18.79
Finance Company	53	35.57
Insurance Company	17	11.41
Hotel	3	2.01
Manufacturing & Processing Company	5	3.36
Trading Company	3	2.01
Other Company	19	12.75
Total	**149**	**100**

(Source: Annual Report 2008/09, NEPSE)

It has been observed that the listed companies in NEPSE have been dominated by finance companies. The number of listed finance companies is 53, which occupies 35.57% of the total listed companies in the fiscal year 2008/09. Next to it, the preponderance of development banks of Nepal is greatest. The number of listed development banks is 28 and occupies 18.79% of the total list. Likewise, 21 commercial banks are listed in NEPSE and thus it covers 14.09% of the total list. Moreover, 17 insurance companies, 3 hotels, 5 manufacturing and processing, 3 trading companies and 19 others have occupied 11.41%, 2.01%, 3.36%, 2.01% and 12.75% respectively.

Figure 4.9

Sector-wise Number of Listed Companies in FY 2008/09
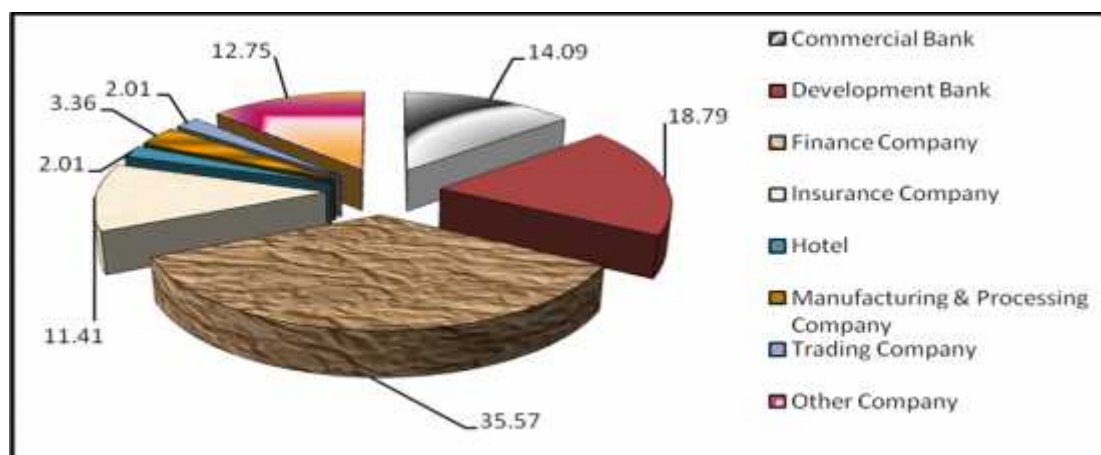
4.1.2.5.2 Stock Turnover in FY 2008/09

The total amount of securities traded in the FY 2008/09 is Rs. 21681.14 million. In the previous fiscal year, however, it is Rs. 22820.76 million. The sector-wise turnover in the FY 2008/09 is presented in the table 4.10:

Table 4.10

Sector-wise Turnover of NEPSE in FY 2008/09

Sector	Turnover	Percentage
Commercial Bank	12406.45	57.22
Development Bank	2740.36	12.64
Finance Company	2615.40	12.06
Insurance Company	212.80	0.98
Hotel	18.69	0.09
Manufacturing & Processing Company	26.08	0.12
Trading Company	33.49	0.15
Other Company	3627.87	16.73
Total	**21681.14**	**100.00**

(Source: Annual Report 2008/09, NEPSE)

It is been ascertained that Commercial Bank sector has the largest turnover of Rs. 12406.45 million, which is 57.22% of the total turnover. Trading amount of Development Bank is Rs. 2740.36 million, which covers only 12.64% of the total. Finance sector has the turnover of Rs. 2615.40 million, which is 12.06% of the total and the Insurance sector covers 0.98% of the total with the turnover of Rs. 212.80 million. The least turnover is of Hotel sector which covers only

0.09% of the total with the turnover of only Rs. 18.69 million. The turnover of Manufacturing & Processing sector is Rs. 26.08 million, which is 0.12% of the total and the trading sector has the turnover of only Rs. 33.49 million with 0.15% of the total. Eventually, the other sectors, which comprises hydropower, mutual fund, preferred stock, promoter shares and other, has the turnover of Rs. 3627.87 million which is 16.73% of the total. Although, the number of listed companies is dominated by the number of finance companies, the turnover of NEPSE depends to commercial banks in great extent. Thus, the role of commercial banks in rendering turnover to the NEPSE is substantial.

Figure 4.10

Sector-wise Turnover in FY 2008/09
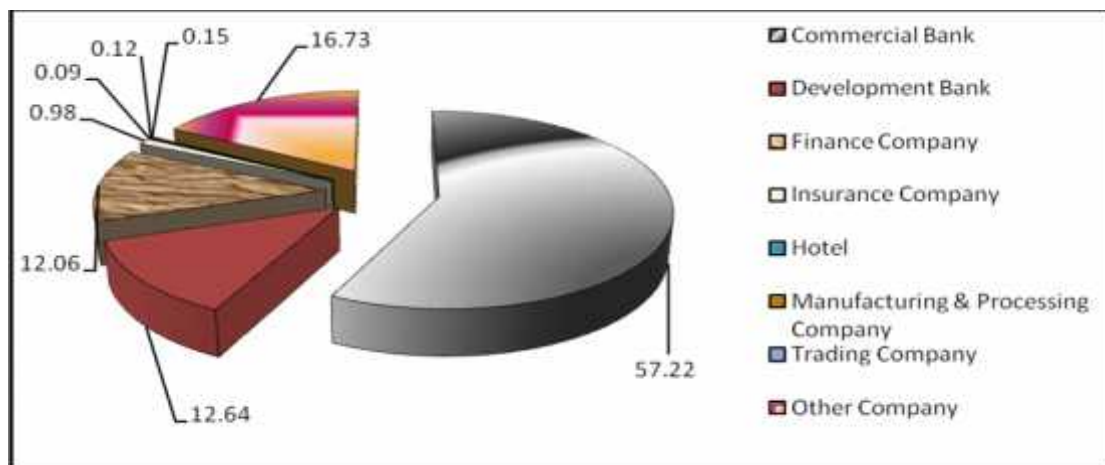
4.1.2.5.3 Market Capitalization of Listed Companies in FY 2008/09

Market capitalization truly depicts the market value of the securities and thus it gauges the interest of investors in various sectors. The market capital of the securities has increased in each fiscal year, indicating high enthusiasm of investors in securities business. By the end of the fiscal year 2008/09, the market capitalization is Rs. 512939.07 millions, which has been comprised by the contribution of various sectors. Thus, to measure the contribution of each sector in increasing the market capital, the sector-wise market capitalization has been analyzed.

Table 4.11
Sector-wise Market Capitalization in FY 2008/09

Sector	Market Capitalization	Percentage
Commercial Bank	192611.17	37.55
Development Bank	16648.39	3.25
Finance Company	17342.23	3.38
Insurance Company	8640.23	1.68
Hotel	3346.41	0.65
Manufacturing & Processing Company	5424.58	1.06
Trading Company	980.70	0.19
Other Company	267945.36	52.24
Total	**512939.07**	**100.00**

(Source: Annual Report 2008/09, NEPSE)

It has been observed that the market capitalization of other sectors, which comprises of hydropower, promoter share, mutual fund, preference share and other, is highest among the 8 sectors. The market capitalization of other companies is Rs. 267945.36 millions, and thus it covers 52.24% of the total market capitalization. Ubiquitously, the contribution of the commercial banks in raising the market capital is substantial, and thus next to the market capitalization of other company, the coverage of commercial banks is greater, which is Rs. 192611.17 millions, representing 37.55% of the total market capital. Similarly, the market capital of finance companies is Rs. 17342.23 millions covering 3.38% of the total market capital. Also, the market capital of development bank is Rs. 16648.39 millions occupying 3.25% of the total market capital. Likewise, the coverage of insurance company, hotel, manufacturing and processing and trading company is 1.68%, 0.65%, 1.06% and 0.19 respectively. Thus, it can be concluded that that the contribution of commercial banks, after other sectors, is quite crucial for enhancing the market capital.

Figure 4.11

Sector-wise Market Capitalization in FY 2008/09
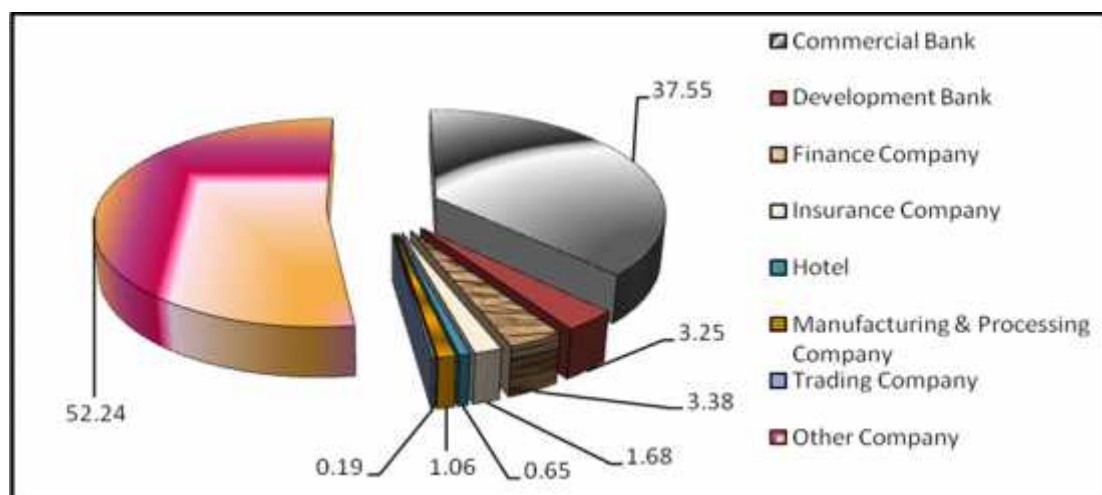
4.1.2.5.4 Monthly NEPSE Index during FY 2008/09

The price index of the listed securities in NEPSE varies frequently in each month, more specifically in each day. Thus, examining the trend of NEPSE index in each month of a year can be helpful in predicting the NEPSE index rise or fall in certain month. The monthly NEPSE index in the fiscal year 2008/09 is presented in the table.

Table 4.12

Monthly NEPSE Index during FY 2008/09

Months	NEPSE Index (Points)
Shrawan	1084.76
Bhadra	976.01
Ashwin	933.97
Kartik	806.90
Mangsir	734.85
Poush	659.81
Magh	663.52
Falgun	667.20
Chaitra	661.27
Baisakh	660.96
Jestha	678.74
Ashad	749.10

(Source: Trading Report 2008/09, NEPSE)

The table depicts that the NEPSE index has followed decreasing trend from Shrawan to Mangsir, i.e. from 1084.76 point to 663.52 point, and then it has slightly increased in Falgun, i.e. 667.20 point, and again it has decreased for the next two months, i.e. 661.27 point in Chaitra and 660.96 point in Baisakh, and finally it has increased for the last two months of the fiscal year 2008/09, i.e. 678.74 point in Jestha and 749.10 point in Ashad. It seems that the NEPSE index rises up from the beginning of the new year to the ending of the fiscal year, assuming fiscal year 2008/09 as the sample year, and thus it can be inferred that the investors become more active within these periods to invest in the securities market.

Figure 4.12

Monthly NEPSE Index during FY 2008/09
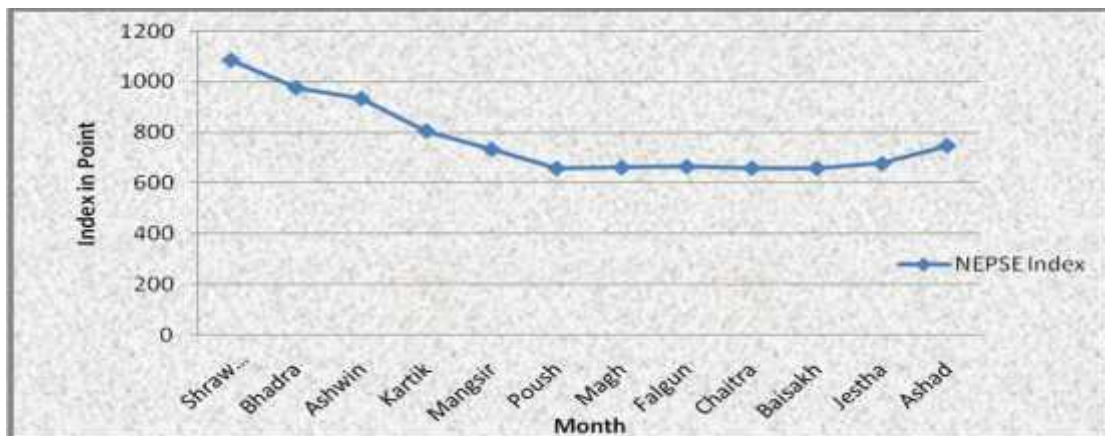
4.1.3 Trend Analysis

To estimate the value of NEPSE index, market capitalization and the stock turnover in the next five year periods, the trend analysis has been conducted, which fulfills the third objective of the study.

4.1.3.1 Trend Analysis of NEPSE Index

The predicted values of NEPSE Index using the trend analysis for the next five fiscal years (from FY 2009/10 to FY 2013/14) are presented in the table.

$$Y = 163.57 + 150.14 \, X$$

Table 4.13

Trend Value of NEPSE Index

Fiscal Year	Trend Value of NEPSE Index
2009/10	1064.40
2010/11	1214.54
2011/12	1364.68
2012/13	1514.82
2013/14	1664.96

(Source: Appendix –III)

The table shows positive relationship between the NEPSE index and the time period, which indicates that along with the lapse of time, the NEPSE index continues to increase. The NEPSE index will be 1064.40 point in the fiscal year 2009/10, and it increases by 150.14 point in each fiscal year, as per the regression line, and thus by the end of the fiscal year 2013/14, the NEPSE index will be 1664.96 point. Thus as per the past trend of NEPSE index, the securities market of Nepal has good prospects in future.

Figure 4.13

Trend Value of NEPSE Index
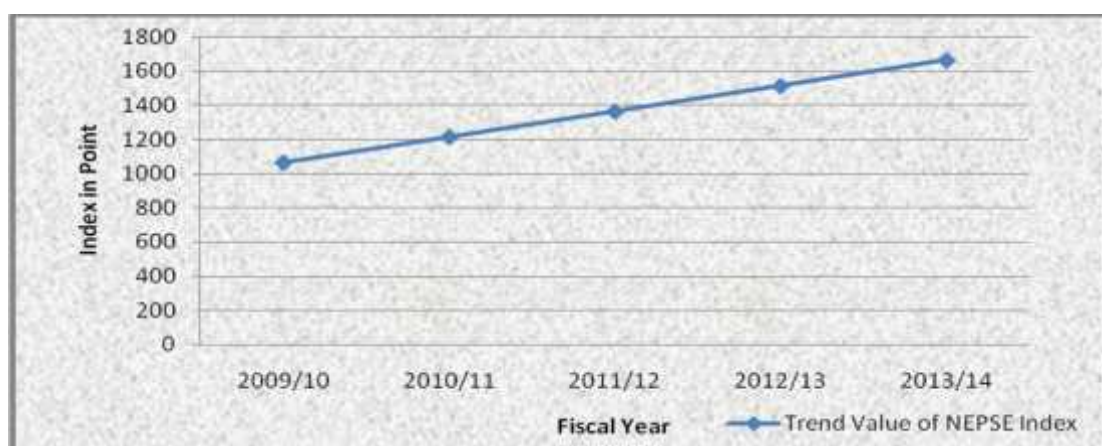
4.1.3.2 Trend Analysis of Market Capitalization

The predicted values of Market Capitalization of NEPSE using trend analysis for the next five fiscal years (from FY 2009/10 to FY 2013/14) are tabulated in the table.

$$Y = -107065.55 + 117263.02 X$$

Table 4.14

Trend Values of Market Capitalization

Fiscal Year	Trend Value of Market Capitalization
2009/10	596512.56
2010/11	713775.58
2011/12	831038.60
2012/13	948301.62
2013/14	1065564.63

(Source: Appendix – III)

The regression line shows that the market capitalization of securities increases with the lapse of time. In each year, the market capitalization of the securities increases by Rs. 117263.02 millions, if the variable -107065.55 remains constant. As a result, estimated value of market capitalization for the fiscal year 2009/10 is Rs. 596512.56 million, which is higher than that of FY 20087/09. In FY 2010/11, the market capitalization is estimated to reach to Rs. 7133775.58 million. Similarly, the predicted value of market capitalization in the FY 2011/12 is Rs. 831038.60 million, in 2012/13 is estimated to be Rs. 948301.62 million and in 2013/14 it is predicted to be Rs. 1065564.63 million. Thus, it can be inferred that the investors will be more enticed toward the securities market and ultimately the market capitalization will be increased in the future.

Figure 4.14

Trend Values of Market Capitalization
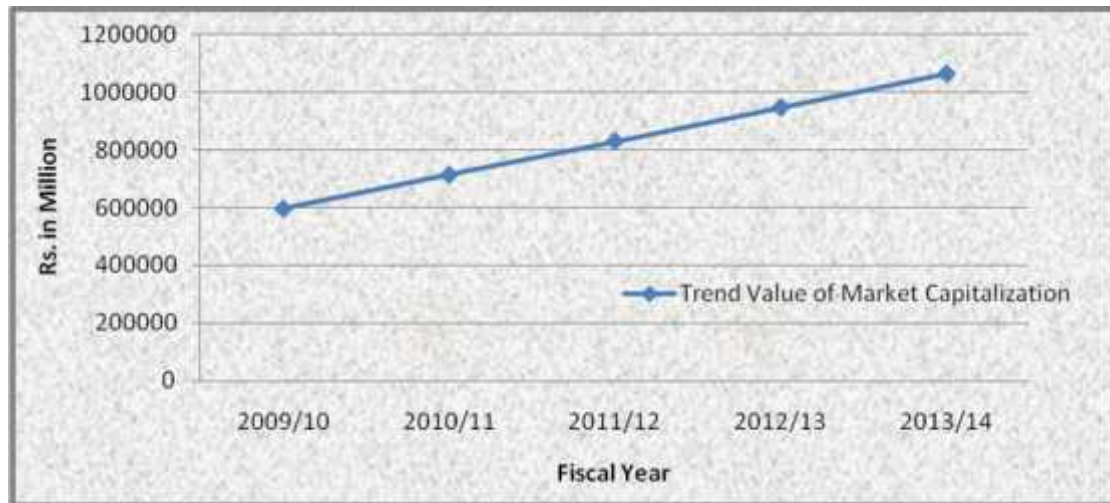
4.1.3.3 Trend Analysis of Stock Turnover

Let Y denotes the dependent variable, turnover and X denotes the independent variable, Year then the predicted values of Turnover of NEPSE using trend analysis for the next five fiscal years (from FY 2008/09 to FY 2012/13) are presented in the table.

$$Y = -1993.22 + 5371.63 \, X$$

Table 4.15

Trend Values of Stock Turnover

Fiscal Year	Trend Value of Stock Turnover
2009/10	30236.53
2010/11	35608.15
2011/12	40979.78
2012/13	46351.40
2013/14	51723.03

(Source: Appendix – III)

The trend analysis shows that in each fiscal year the turnover of NEPSE increases by Rs. 5371.63 millions, if the variable -1993.22 remain constant. The table delineates that the predicted value of turnover will be Rs. 30236.53 million in the FY 2009/10, which is estimated to increase to Rs. 35608.15 million in the FY 2010/11. Likewise, it is estimated to reach to Rs. 40979.78, Rs. 46351.40 million and Rs. 51723.03 million in the FY 2011/12 FY 2012/13 and FY 2013/14 respectively.

Figure 4.15

Trend Values of Stock Turnover
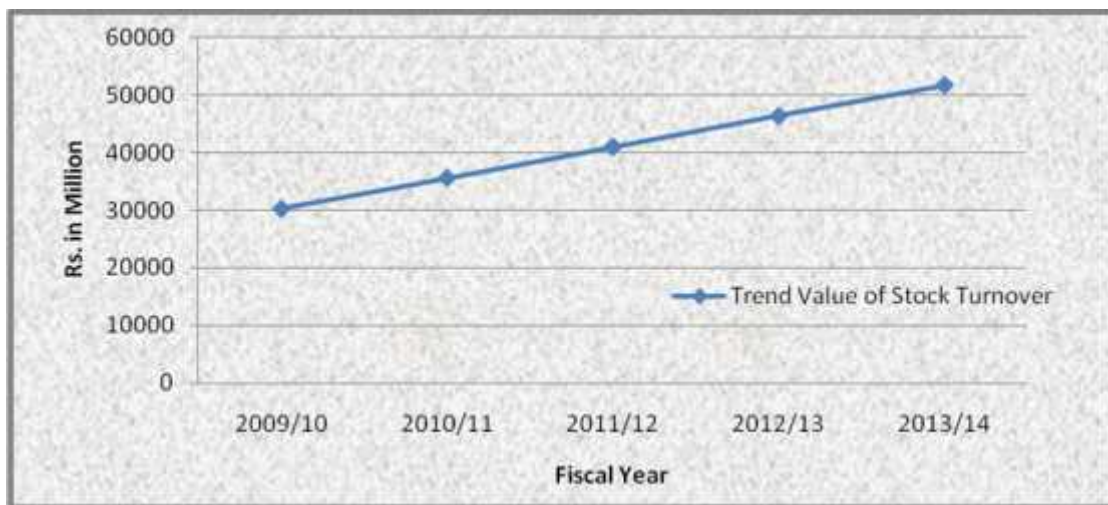
4.2 Primary Data Analysis

To analyze the opinions related to the securities market, the primary data have been collected by conducting the questionnaire. For this a questionnaire containing 11 questions has been prepared and requested to the 10 personnel of securities brokers, 15 investors and 15 students. However, 3 personnel of securities brokers and 1 student have not responded and thus the responses have been collected from remaining 7 personnel of brokers, 15 investors and 14 students.

4.2.1 Efficiency of Security Market

To detect whether the security market provides up to date information and it is operating efficiently, the respondents are requested to express their opinions. The different opinions obtained from them are presented in the following table.

Table 4.16

Efficiency of Security Market

Response	Responses			Total	
	Brokers	Investors	Student	No.	%
Yes	6	12	9	27	75
No	1	2	2	5	14
Don't Know	0	1	3	4	11
Total	**7**	**15**	**14**	**36**	**100**

(Source: Opinion Survey, 2010)

The above table shows that the majority of the respondents, 27 out of 36, said that the Nepalese Security market is informational and operationally efficient. Analyzing on each category, the majority of each group; 6 out of 7 personnel of brokerage firms, 12 out of 15 investors, 9 out of 14 students, have strongly affirmed that Nepalese security market is efficient. Only 14% of the respondents have said that the security market is not efficient in operation and does not provide effective information. However, 11% respondents have remained neutral on this query. Considering the majority, 75% respondents, it can be concluded that the stock market of Nepal is informational and operationally efficient in the present context and thus should be enhanced in the future.

Figure 4.16

Efficiency of Security Market (Total)
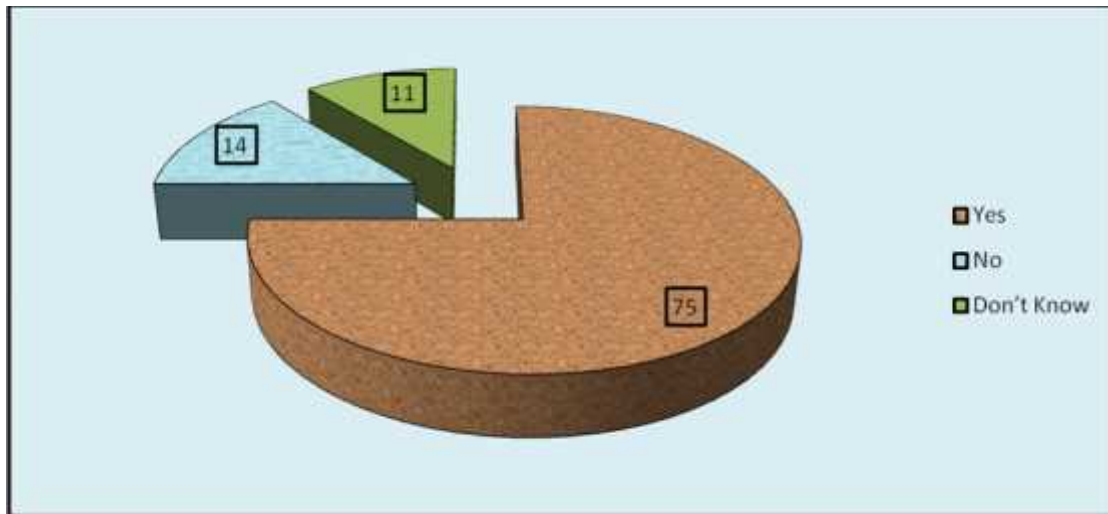
4.2.2 Desire for Investment

To trace out the main crave for which the investors makes investment on security, only the investors are asked about their desire for investment. As the question is related with the investors only, the other respondents are ignored on this question. The responses obtained from the investors are depicted in the following table.

Table 4.17

Desire for Investment

Response	Investors	
	No.	**%**
Social Status	1	7
Dividend	10	66
Friend and Family	1	7
Stock Broker	1	7
Marketability	2	13
Total	**15**	**100**

(Source: Opinion Survey, 2010)

The above table delineates that the majority of the investors makes decision on the basis of dividend distribution pattern of the company. About 66% of the

investors are craved to invest on security market by the dividend. Similarly, 1 out of 15 (7%) makes investment to gain social status, 1 out of 15 (7%) makes investment on the suggestions of friend and family, 1 out of 15 (7%) makes investment on the advice of stock broker and 2 out of 15 (13%) makes investment by analyzing the ease marketability of the security. Thus, on the basis of the majority, it can be concluded that the investors are highly craved to invest by dividend structure of the company and eventually to generate income.

Figure 4.17

Desire for Investment
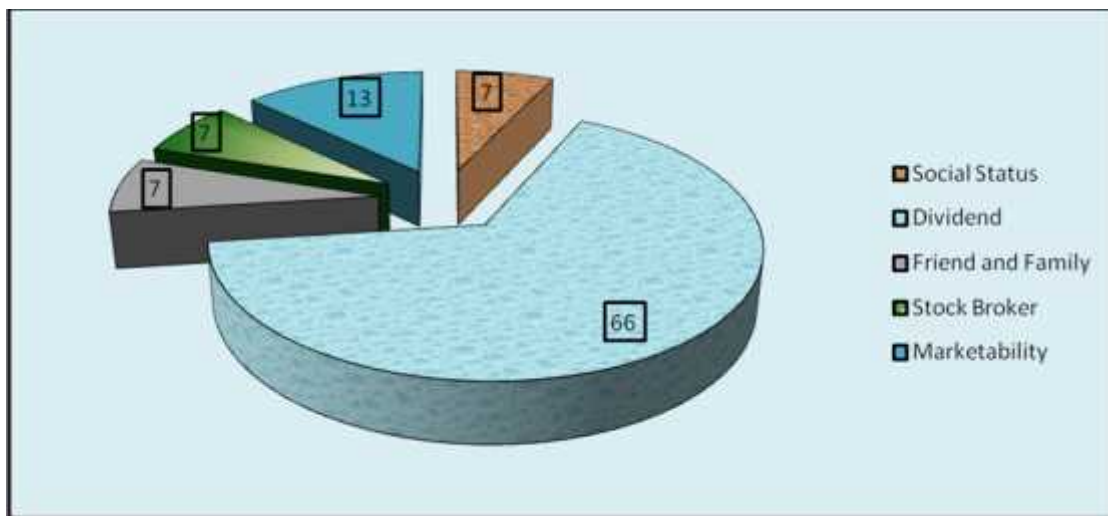
4.2.3 Basis to Invest in Secondary Market

To know the basis of investment in the Secondary Market, both investors, and students, who are likely to be potential investors, are asked on this matter. To draw the exact basis, the personnel of brokers have been excluded from this question. The different opinions obtained from the investors and students are presented in the following table.

Table 4.18

Basis to Invest in Secondary Market

Response	Responses		Total	
	Investors	Students	No.	%
NEPSE Index	6	6	12	41
Closing Price	1	0	1	3
Turnover	0	0	0	0
Company's Goodwill	1	1	2	7
Company's Profit	3	2	5	17
Dividend Payout Ratio	4	5	9	31
Total	**15**	**14**	**29**	**100**

(Source: Opinion Survey, 2010)

The above table shows that 12 respondents have stated that investors invest on secondary market by analyzing the trend of NEPSE index. Similarly, 9 respondents have opined that investors invest by gauging the dividend payout ratio of the company, 5 respondents have said that investors invest by analyzing the considering the company's profit, 2 respondents have avowed that investors invest on the basis of company's goodwill and 1 on the basis of closing price. Since, the majority of the respondents (41%) have stated that investors invest on the basis of NEPSE Index, it can be considered that NEPSE index is the major basis for share investment in secondary market.

Figure 4.18

Basis to Invest in Secondary Market (Total)
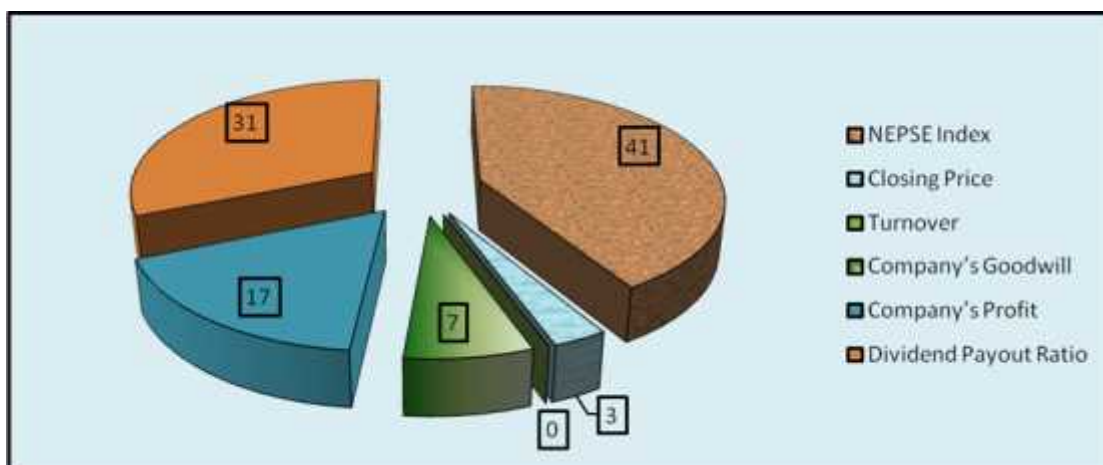
4.2.4 Awareness of Investors

Full Awareness of investors about the security trading system is most crucial for the growth of security. Hence, to examine whether investors are fully aware about the Nepalese Security Trading System, the respondents were asked to express their view on this regard. The different opinions obtained from the respondents are presented in the following table.

Table 4.19

Awareness of Investors

Response	Responses			Total	
	Brokers	Investors	Student	No.	%
Yes	4	6	5	15	42
No	3	8	7	18	50
Don't Know	0	1	2	3	8
Total	**7**	**15**	**14**	**36**	**100**

(Source: Opinion Survey, 2010)

The above table has shown that the majority of the respondents, 18 out of 36, opined that the investors are not fully aware about the Nepalese security trading system. However, the majority of the personnel of brokerage firms, 4 out of 7, have affirmed that the investors are fully aware about the security trading system. In contrast, the majority of the investors, 8 out of 15, and the majority of the students, 7 out of 14, have strongly stated that the investors are not fully aware about the trading system. Hence, mixed opinion is obtained on the full awareness of investors. Eventually, considering the overall majority (50%), half of the respondents, it can be concluded that the investors are not fully aware about Nepalese Security Trading System and thus SEBON should conduct different programs and seminars to fully aware investors and eventually increase turnover.

Figure 4.19

Awareness of Investors (Total)
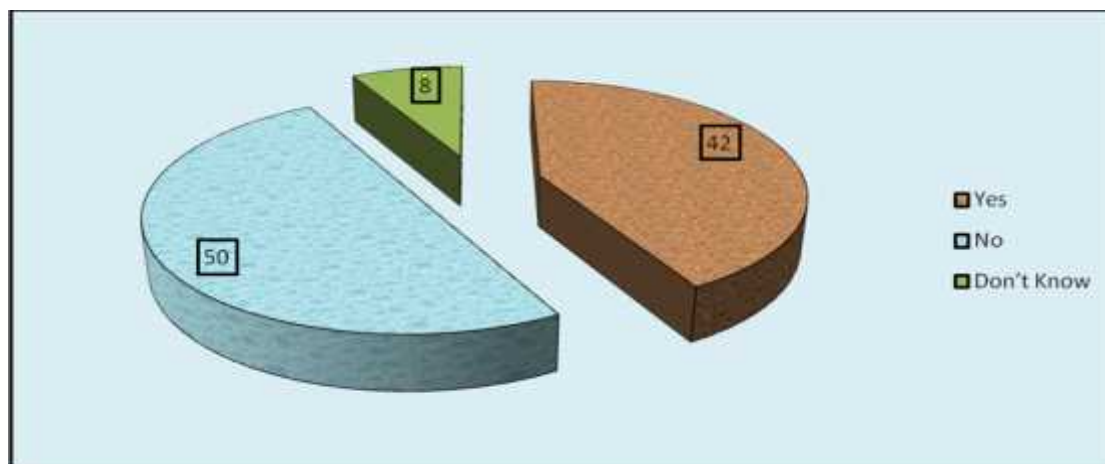
4.2.5 Satisfaction on Securities Trading System

To investigate the level of satisfaction on the present securities trading system in Nepal, the respondents were asked whether they are satisfied with the trading system. The responses achieved from them are presented in the following table.

Table 4.20

Satisfaction of Securities Trading System

Response	Responses			Total	
	Brokers	**Investors**	**Student**	**No.**	**%**
Yes	6	9	8	23	64
No	1	6	4	11	31
Don't Know	0	0	2	2	6
Total	**7**	**15**	**14**	**36**	**100**

(Source: Opinion Survey, 2010)

The above table has shown that out of 7 personnel of brokerage frims, 6 are satisfied with the existing trading system, however 1 is not satisfied with the trading system. Similarly, 9 investors are satisfied and 6 are not satisfied and 8 students are satisfied, 4 are not satisfied and 2 has remained neutral on the satisfaction of existing securities trading system. In overall, 64% of the respondents are satisfied, 31% are not satisfied and 6% remained neutral. As

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the majority of the respondents, 23 out of 36, are satisfied with the securities trading system, it can be considered that the appropriate trading system is followed in NEPSE and there is good prospect of security market in future as well.

Figure 4.20

Satisfaction of Securities Trading System (Total)
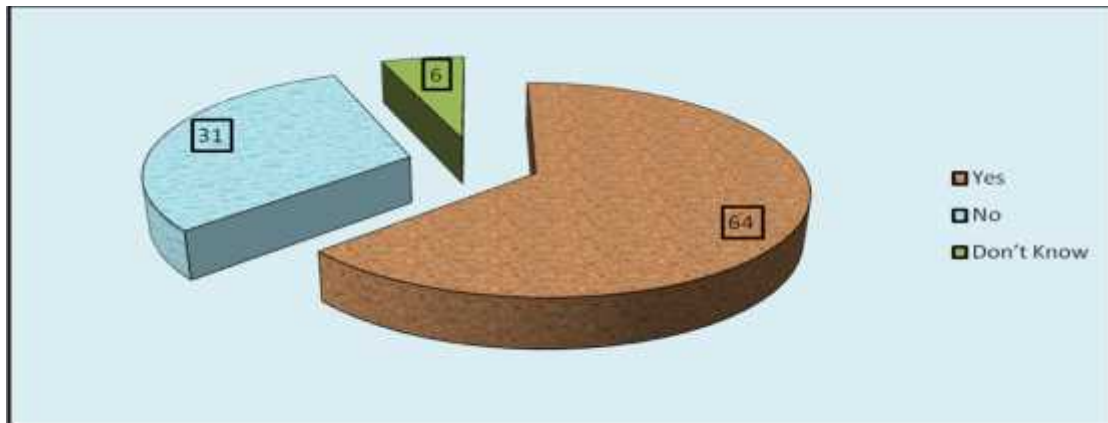
4.2.6 Influencer of Security Price

The investors are attracted in the security of companies by analyzing various factors. Such factor creates rise or fall in the security price. To examine which factor most influence the investor on buying security of certain company and influences the security price of the listed company, the respondents were asked on this regard. The opinions obtained from them are presented in the following table.

Table 4.21

Influencer of Security Price

Response	Responses			Total	
	Brokers	Investors	Student	No.	%
Dividend	4	10	8	22	61
Rumor	0	0	2	2	6
Financial Condition	2	2	3	7	19
Management	1	3	1	5	14
Total	**7**	**15**	**14**	**36**	**100**

(Source: Opinion Survey, 2010)

The above table depicts that the majority of the respondents, 22 out of 36 (61%), have stated that dividend is the most influencing factor of security price. Similarly, 6%, 19% and 14% of the respondents affirmed that rumor, financial situation of the company and management of the company respectively are the influencing factors of the security price. Analyzing each category, the majority of each category; 4 out of 7 brokers, 10 out of 15 investors and 8 out of 14 students, have stated that dividend is the main factor that moves the security price. Hence, it can be concluded that dividend distribution pattern of the company is the major motive behind investing on the share of certain company and which raises or falls the security price.

Figure 4.21

Influencer of Security Price (Total)
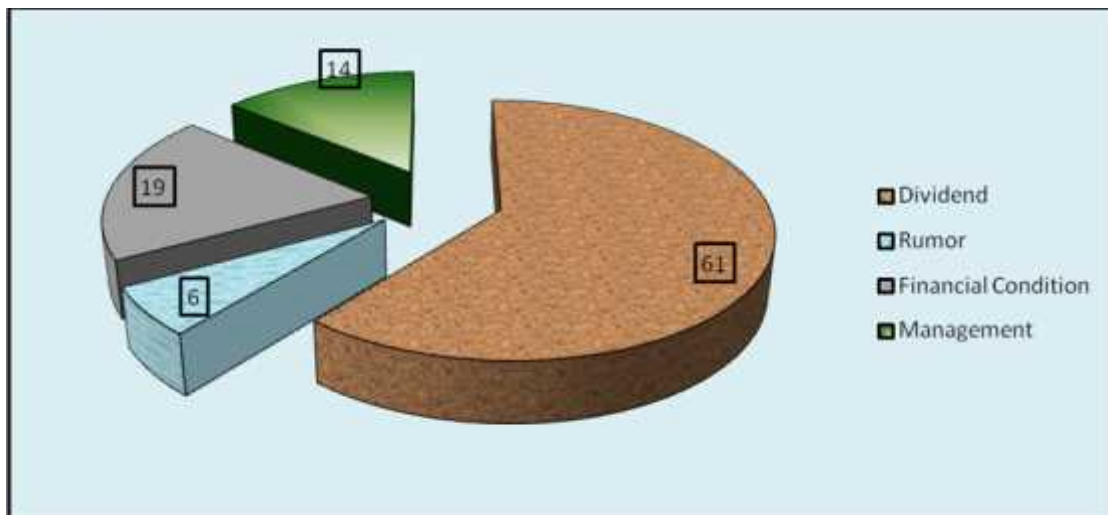
4.2.7 Effects of Rules and Regulations of SEBON

To determine whether the rules and regulations of SEBON affect the security value, the respondents were asked on this matter. The answers achieved from them have been presented in the following table.

Table 4.22

Effects of SEBON

Response	Responses			Total	
	Brokers	**Investors**	**Student**	**No.**	**%**
Yes	4	8	5	17	47
No	2	3	6	11	31
Don't Know	1	4	3	8	22
Total	**7**	**15**	**14**	**36**	**100**

(Source: Opinion Survey, 2010)

The table shows that the majority of the respondents, 17 out of 36, have stated that the rules and regulations of SEBON causes rise or fall on security value of the company. However, 31% respondents (11 out of 36) have affirmed that there is no relationship between rules and regulations of SEBON and the value of security. Likewise, 22% respondents (8 out of 36) have remained neutral on this matter. Looking each category, the majority of brokers, 4 out of 7, and investors, 8 out of 15, opined that the rules and regulations affect the security value. However, the majority of the students, 6 out of 14, have stated that stock value is not affected by such rules and regulations. Rather mixed opinion has been obtained in this matter. Hence, analyzing the overall majority, 47% respondents and the experience of respondents engaged in share transactions, it can be concluded that the rules and regulations of SEBON directly affect the security price.

Figure 4.22

Effects of SEBON (Total)
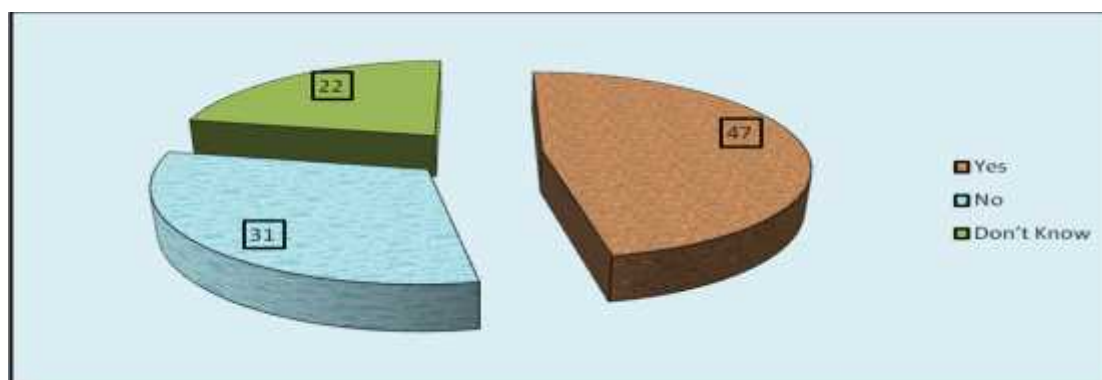
4.2.8 Problems of Securities Trading System

Many factors are hindering the security trading in Nepal. To detect which factor barricades most in the trading system of Nepal, the respondents are asked to express their view. The responses obtained from them are presented in the following table.

Table 4.23

Problems of Stock Market Growth

Problems	Basis	Rank						Total	Weight	Mean Wt.	Overall Rank
		1	2	3	4	5	6				
Small Capital Market	Total	8	15	6	7	0	0	36	84	2.33	2
	Brokers	2	4	1	0	0	0	7	13	1.86	2
	Investor	4	4	3	4	0	0	15	37	2.47	2
	Student	2	7	2	3	0	0	14	34	2.43	2
Lack of Investor's Confidence	Total	20	14	2	0	0	0	36	54	1.50	1
	Brokers	4	3	0	0	0	0	7	10	1.43	1
	Investor	7	8	0	0	0	0	15	23	1.53	1
	Student	9	3	2	0	0	0	14	21	1.50	1
Lack of Proper Knowledge	Total	0	0	4	7	14	11	36	176	4.89	6
	Brokers	0	0	2	0	3	2	7	33	4.71	5
	Investor	0	0	0	4	7	4	15	75	5.00	6
	Student	0	0	2	3	4	5	14	68	4.86	5
Lack of Coordination	Total	0	1	5	8	5	17	36	176	4.89	5
	Brokers	0	0	1	3	1	2	7	32	4.57	4
	Investor	0	1	3	1	2	8	15	73	4.87	5
	Student	0	0	1	4	2	7	14	71	5.07	6
Inappropriate Rules and regulations	Total	4	4	11	9	3	3	36	120	3.33	3
	Brokers	0	0	2	4	1	0	7	27	3.86	3
	Investor	1	0	5	4	2	3	15	60	4.00	4
	Student	3	4	6	1	0	0	14	33	2.36	3
Restriction on Foreign Investors	Total	4	2	6	5	14	5	36	146	4.06	4
	Brokers	1	0	1	0	2	3	7	32	4.57	4
	Investor	3	2	4	2	4	0	15	47	3.13	3
	Student	0	0	1	3	8	2	14	67	4.79	4

(Source: Opinion Survey, 2010)

The above table shows that lack of investor's confidence is the major problem that is barricading the security trading system in Nepal. The respondents have ranked 1 for lack of investor's confidence, 2 for small capital market, 3 for Inappropriate rules and regulations, 4 for restriction of foreign investors, 5 for lack of coordination among monitoring bodes of stock market and 6 for lack of proper knowledge on investors. Looking individually as well, the majority of each group, 4 out of 7 brokers, 7 out of 15 investors and 9 out of 14 students, have ranked 1 for lack of confidence in investors, which has indicated that the lack of investor's confidence is the major hindrance in securities trading system of Nepal. Besides this, small capital market is also the next problem of trading system.

4.2.9 Prospects of Security Market

NEPSE has adopted various techniques for the enhancement of security market in Nepal. So to examine which method is appropriate for the amelioration of securities trading system, the respondents are asked to express their opinions.

Table 4.24
Prospects of Security Market

Prospects	Basis	Rank											Total	Weight	Mean Wt.	Overall Rank
		1	2	3	4	5	6	7	8	9	10	11				
Automated Trading System	Total	3	2	4	9	11	4	3	0	0	0	0	36	155	4.31	4
	Brokers	1	1	1	2	2	0	0	0	0	0	0	7	24	3.43	4
	Investor	2	1	0	5	3	2	2	0	0	0	0	15	65	4.33	4
	Student	0	0	3	2	6	2	1	0	0	0	0	14	66	4.71	4
Recruitment of New Employee	Total	0	0	1	1	5	15	6	6	2	0	0	36	230	6.39	6
	Brokers	0	0	1	0	0	1	2	2	1	0	0	7	48	6.86	7
	Investor	0	0	0	1	3	6	2	3	0	0	0	15	93	6.20	6
	Student	0	0	0	0	2	8	2	1	1	0	0	14	89	6.36	5
Trading through WAN	Total	0	0	0	1	7	7	10	5	3	3	0	36	248	6.89	7
	Brokers	0	0	0	0	1	3	3	0	0	0	0	7	44	6.29	6
	Investor	0	0	0	0	3	3	5	1	3	0	0	15	103	6.87	7
	Student	0	0	0	1	3	1	2	4	0	3	0	14	101	7.21	6
Market Halt Introduced	Total	0	0	0	0	4	0	3	7	4	11	7	36	320	8.89	9
	Brokers	0	0	0	0	1	0	1	2	0	3	0	7	58	8.29	9
	Investor	0	0	0	0	2	0	1	5	1	6	0	15	126	8.40	9
	Student	0	0	0	0	1	0	1	0	3	2	7	14	136	9.71	9
Extended Trading Hours	Total	3	1	8	10	4	4	2	0	2	0	2	36	167	4.64	5
	Brokers	0	0	0	2	1	2	1	0	1	0	0	7	41	5.86	5
	Investor	1	0	4	4	3	0	0	0	1	0	2	15	75	5.00	5
	Student	2	1	4	4	0	2	1	0	0	0	0	14	51	3.64	3
Real Time Information	Total	0	0	0	0	0	0	2	1	11	15	7	36	348	9.67	10
	Brokers	0	0	0	0	0	0	0	0	4	2	1	7	67	9.57	10
	Investor	0	0	0	0	0	0	0	1	3	7	4	15	149	9.93	10
	Student	0	0	0	0	0	0	2	0	4	6	2	14	132	9.43	8
Promoter's shares Traded	Total	0	0	0	0	1	5	8	14	7	1	0	36	276	7.67	8
	Brokers	0	0	0	0	1	1	0	3	1	1	0	7	54	7.71	8
	Investor	0	0	0	0	0	4	3	5	3	0	0	15	112	7.47	8
	Student	0	0	0	0	0	0	5	6	3	0	0	14	110	7.86	7
OTC Market Started	Total	6	4	9	11	3	1	2	0	0	0	0	36	120	3.33	3
	Brokers	1	1	2	2	1	0	0	0	0	0	0	7	22	3.14	3
	Investor	3	2	6	2	0	0	2	0	0	0	0	15	47	3.13	3
	Student	2	1	1	7	2	1	0	0	0	0	0	14	51	3.64	3
Profit Seeking NEPSE	Total	10	11	11	3	1	0	0	0	0	0	0	36	82	2.28	2
	Brokers	2	1	3	1	0	0	0	0	0	0	0	7	17	2.43	2
	Investor	4	5	3	2	1	0	0	0	0	0	0	15	36	2.40	2
	Student	4	5	5	0	0	0	0	0	0	0	0	14	29	2.07	2
Monthly Publication	Total	0	0	0	0	0	0	0	3	7	6	20	36	367	10.19	11
	Brokers	0	0	0	0	0	0	0	0	0	1	6	7	76	10.86	11
	Investor	0	0	0	0	0	0	0	0	4	2	9	15	155	10.33	11
	Student	0	0	0	0	0	0	0	3	3	3	5	14	136	9.71	10
Increasing Interest	Total	14	18	3	1	0	0	0	0	0	0	0	36	63	1.75	1
	Brokers	3	4	0	0	0	0	0	0	0	0	0	7	11	1.57	1
	Investor	5	7	2	1	0	0	0	0	0	0	0	15	29	1.93	1
	Student	6	7	1	0	0	0	0	0	0	0	0	14	23	1.64	1

(Source: Opinion Survey, 2010)

The above table shows that the increasing interest of investors on security market is the most important prospects of security market in Nepal. The respondents have ranked 1 for increasing interest of investors, 2 for the conversion of NEPSE into profit oriented, 3 for the starting of OTC market, 4

for launching automated trading system, 5 for extending trading hours, 6 for recruitment of new employee, 7 for trading through WAN system, 8 for trading of Promoter's share, 9 for the introduction of Market Halt system, 10 for the dissemination of real time and 11 for monthly market review publication. In overall, the majority of the respondents, 14 out of 36, have opined that the increasing interest of educated people toward security market is the most important factor for raising the prospect of security market in Nepal.

4.2.10 Malpractices in Security Market

The malpractices in share market have created the uncertainty in the stock price. General investors are facing huge losses from the malpractices existing in the stock market and obviously abolishing the effective securities trading system. To examine which of the major malpractices is causing problem in the securities trading system, the respondents are asked to express their opinions on the basis of their past experience in security trade.

Table 4.25
Malpractices in Security Market

Malpractices	Basis	Rank						Total	Weight	Mean Wt.	Overall Rank
		1	2	3	4	5	6				
Pooling	Total	18	11	5	2	0	0	36	63	1.75	1
	Brokers	4	2	1	0	0	0	7	11	1.57	1
	Investor	8	5	1	1	0	0	15	25	1.67	1
	Student	6	4	3	1	0	0	14	27	1.93	1
Cornering or Warehousing	Total	2	1	7	15	9	2	36	142	3.94	4
	Brokers	0	0	1	4	2	0	7	29	4.14	4
	Investor	1	0	3	4	5	2	15	63	4.20	5
	Student	1	1	3	7	2	0	14	50	3.57	3
Organized Runs	Total	5	6	11	12	2	0	36	108	3.00	3
	Brokers	1	1	3	2	0	0	7	20	2.86	3
	Investor	2	2	3	7	1	0	15	48	3.20	3
	Student	2	3	5	3	1	0	14	40	2.86	2
Ramping	Total	0	0	0	1	7	28	36	207	5.75	6
	Brokers	0	0	0	0	2	5	7	40	5.71	6
	Investor	0	0	0	1	2	12	15	86	5.73	6
	Student	0	0	0	0	3	11	14	81	5.79	5
Washsale	Total	10	16	7	1	2	0	36	77	2.14	2
	Brokers	2	4	1	0	0	0	7	13	1.86	2
	Investor	3	6	4	0	2	0	15	37	2.47	2
	Student	5	6	2	1	0	0	14	27	1.93	1
Insider Training	Total	1	2	6	5	16	6	36	159	4.42	5
	Brokers	0	0	1	1	3	2	7	34	4.86	5
	Investor	1	2	4	2	5	1	15	56	3.73	4
	Student	0	0	1	2	8	3	14	69	4.93	4

(Source: Opinion Survey, 2010)

The above table shows that pooling, buying and selling shares within a group, is a major malpractice in the existing security trading system. The respondents have ranked 1 for pooling, 2 for washsale, 3 for organized runs, 4 for cornering or warehousing, 5 for insider training and 6 for ramping. The stock exchange of Nepal should introduce new rule and regulations to control such malpractice. The introduction of fines and penalties is essential for the person committing such malpractice. Effective administration by NEPSE can control such malpractices and also keeping very confidential the unpublicized decision of the listed company can also control the malpractice like insider training.

4.2.11 Responsible for Appropriate Trading System

To know who is most responsible for the appropriate trading system in the security market, the respondents are asked to opine their views. The opinions obtained from them are depicted in the following table.

Table 4.26

Responsible for Appropriate Trading System

Response	Responses			Total	
	Brokers	**Investors**	**Student**	**No.**	**%**
Investors	0	0	0	0	0
Brokers	0	1	0	1	3
NEPSE	3	5	6	14	39
SEBON	4	9	8	21	58
Total	**7**	**15**	**14**	**36**	**100**

(Source: Opinion Survey, 2010)

The above table shows that the majority of the respondents, 21 out of 36, have strongly stated that SEBON should be responsible for appropriate trading system in the security market. However, 14 out of 36 (39%) have said that NEPSE should be responsible and 1 professional investor (3%) has blamed that brokers should be responsible for appropriate trading system in the security market. Also analyzing each category, it has been found that the majority in each group, 4 out of 7 brokers, 9 out of 15 investors and 8 out of 14 students,

have pointed out SEBON to be responsible for appropriate trading practices in the stock market. Hence, looking the overall majority (58%), it can be concluded that SEBON is the major regulating body in effective trading system, however, the responsibility of other bodies cannot be neglected completely. So, for appropriate system each participant should contribute equally.

Figure 4.23

Responsible for Appropriate Trading System (Total)
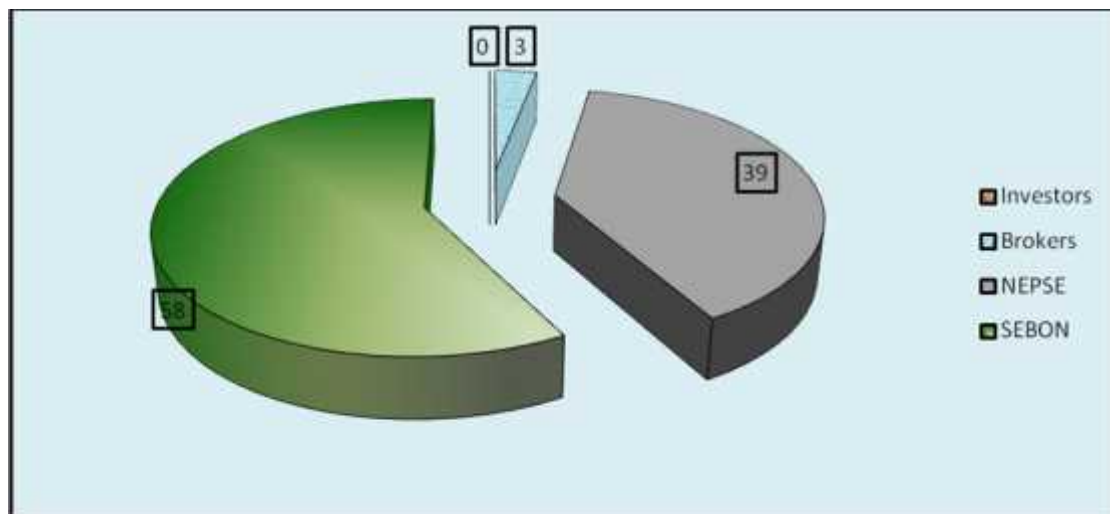
4.3 Major Findings of the Study

On the basis of the analysis of the collected data, the following major findings have been drawn;

Findings from Secondary Data

ʃ The NEPSE index has followed increasing trend for the first four observed periods and then it has decreased in the fiscal year 2008/09. The NEPSE index at the end of the fiscal year 2008/09 is 749.10 points.

ʃ The total turnover of the NEPSE has increased from Rs. 4657.68 millions in the fiscal year 2004/05 to Rs. 42166.14 millions in the fiscal year 2008/09. The turnover from stock is greater than the turnover from bond.

⎰ The market capitalization of securities has increased from Rs. 61365.89 millions in the fiscal year 2004/05 to Rs. 512939.07 millions in the fiscal year 2008/09. The market capitalization has crucial role to upgrade the gross domestic product of the nation.

⎰ By the end of the fiscal year 2008/09, the number of listed companies is 149. However, within the observed periods, 12 companies are delisted in the fiscal year 2006/07 and 5 companies are delisted in the fiscal year 2007/08.

⎰ In average, 87.35% of the total listed companies have been traded within the observed periods. The number of traded companies at the end of the fiscal year 2008/09 is 137.

⎰ The market capitalization ratio is 31.03% of the total GDP in average. Similarly, the stock turnover has represented 1.82% of the total GDP. And the stock turnover to market capitalization is 6.22%.

⎰ The number of listed companies has been dominated by the number of finance companies. However, the turnover of the NEPSE is dominated by the turnover from securities transaction of commercial banks, which occupies 57.22%.

⎰ The trend analysis indicates that the NEPSE index, market capitalization and turnover have positive relationship with the lapse of times. And thus all these three variables are going to increase in the future.

Findings from Primary Data Analysis

⎰ The majority of the respondents, 75%, have stated that the securities market of the country is efficient. 66% of the investors said that they invest share to gain dividend and also dividend is the most influencing factor that fluctuates security price. 41% of respondents have stated that investors analyzes NEPSE index before making investment in the secondary market.

⎰ Half of the respondents have stated that the investors are not fully aware of the practices of securities trading system. Likewise, 64% of the

respondents said that the investors are satisfied with the existing security trading system. Also, 47% of the respondents are of the opinion that the rules and regulations of SEBON affect the value of security.

⟩ Similarly, lack of investor's confidence is the major problem of trading system. Also, the growing interest of the educated people in the security market is the major prospects of security market in Nepal.The major malpractice, pooling, is widespread in security market and thus is creating uncertainty in security price. Besides pooling, washsale is also equally practiced.

⟩ Finally, 58% of the respondents stated that SEBON should be responsible for appropriate trading system in security market.

CHAPTER – V
SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Summary

Securities markets play a crucial role in economic growth and financial stability. The primary purpose of securities markets is to serve as a mechanism for the transformation of savings into financing for the real sector, thus constituting an alternative to bank financing. Markets provide the best (albeit sometimes imperfect) mechanism for asset pricing. Markets are also a mechanism through which risk is transferred and risk exposure diversified—which allows firms to unlock capital for new investments. Risk transfer and pricing mechanisms in the market allow financial institutions, such as banks and insurance companies, to manage risk more efficiently; and markets may therefore work as a buffer for disruption of banking system and therefore contribute to financial stability. The more efficient markets are, the better these outcomes are achieved and the greater the contribution to the economy.

While the role of securities markets is more meaningful in developed economies, there is evidence of the growing importance of securities markets in emerging market and developing countries. In many emerging market and developing countries, securities markets are beginning to gain a place as a source of financing for the corporate sector, although in most markets this is initially restricted to the larger corporate players. Along with private and public pension funds, collective investment schemes have become important players in many developing and emerging market countries and their demand for suitable investments is driving development.

Stock exchange is the backbone of economy and Nepal is not an exception. Development of vivacious and dynamic stock exchange is the pre-requisite for the upliftment of the economic conditions of the country. Hence, the development of efficient stock exchange becomes essential to assist in the

development of the whole economy. So the promotion of the stock exchange in a sizeable extent would promote the economic development through increased mobilization of saving and their channeling into productive sectors, and thereby creating suitable economic outcomes in the economy.

Securities trading system is the main function performed by a stock exchange. The security exchange should follow sound trading system for the effective and efficient trading of the securities. The securities trading systems in NEPSE still has different deficiencies like low trading volume, absence of professional brokers, early stage of growth, limited movement of share prices, limited information to investors, price instability, lack of sound investment decisions of the investors, etc. Furthermore, due to the slow growth of corporate sector in the country, stock market of Nepal is not developing as expected. In this light, this study was carried out mainly focusing on the securities market of Nepal. For this, NEPSE has been taken as the main source of data.

5.2 Conclusion

The instability of the government, strike, malpractices in the stock market, investors' interest to other sectors like real estate and others have greatly influenced the securities market of Nepal in the recent year and thus the NEPSE index has been diminished. Despite this, it can be concluded that the affectionate of the securities market in investors have been growing in greater extent and thus investors are defraying more market price for taking the possession on shares. The increasing trend of market capitalization indicates increase in market price per share of the companies listed, which indicates positive impact of securities market on the investors.

The number of listed companies has almost been in increasing trend although the growth trend has decreased. This indicates that the NEPSE might have incorporated most of the institutions and thus there is slow growth in listing. Observing the company traded to listed ratios, it can be assumed that NEPSE

should monitor the obstacles in the market that are preventing the listed companies to remain untraded. Further, it can be concluded that market capitalization has substantial role to stimulate the GDP growth.

Moreover, the development of securities market has crucial role to upgrade the GDP and thus buttress the economy of the country. Thus for the economic prosperous of the country, the uplift in annual turnover of securities market is quite necessary. Although, the listed companies in NEPSE has been highly dominated by finance companies, the contribution of commercial banks in generating turnover is highest, and the market capitalization of other institutions, which comprises hydropower, promoter share, mutual fund, preference share and other is strongest.

Similarly, from the primary data analysis, it can be concluded that the existing trading system is in satisfactory condition. And the lack of investors' confidence is the major hindrance of the trading system. Also, it can be concluded that the malpractices like pooling, washsale and others are widespread in stock market, which are indirectly breaking the confidence of general investors. However, the interest shown by the educated person on the security market indicated the good future of security trading in Nepal. Also, it can be concluded that the investors invest with the objective of gaining primarily dividend and thus dividend is the prime factor that influences share price. Also, the investors considers primarily NEPSE index before investing in security.

5.3 Recommendations

After analyzing the securities market, the following recommendations have been provided for the enhancement of the securities market;

⟩ NEPSE should regularly update the information furnished by the listed companies and analyzed timely. If any company is found working against NEPSE rules, the company should be immediately taken into

action. The NEPSE should have high speed settlement and clearance system, investor-friendly environment, well-equipped office, computerized system and efficient staff. NEPSE should also focus towards the possibility of substitution of present trading mechanism by electronic trading system.

) For the development of securities market in Nepal, more institutional investors are needed and developed so that the small investors could also participate in investing in the shares of different companies. NEPSE should also start the trading of different bonds and debentures including governmental bonds, because these fixed-rate yielding securities are very essential to construct the sound portfolio for the investors.

) Generally, Nepalese investors are not aware of their investment scheme. Therefore, they should be made aware of the investment scheme on the basis of proper analysis of risk and return. Investors should always be aware of their strength and weakness and risk-taking capabilities so that superior forecasting and sound understanding of stocks may give winning edge to them.

) Nepalese investors lack proper knowledge of stock markets. They should, therefore, need to read daily newspapers and journals and annual reports of NESPE and SEBON. They provide extensive statistical data and financial news which may, in turn, increase the forecasting capabilities of the investors. The investors should always be sensitive especially to developments in stock price and volume traded of the listed companies.

) The stock brokers should be professional to enhance the awareness among the investors. They should be friendly towards the investors by furnishing them with sufficient and reliable information and suggestions.

) Information brochure should be modified timely to ensure fair share transactions. Studies should be conducted to inform investors regarding

compliance of legal provisions. Other relevant studies to bring into light on the performance of the listed companies are also necessary.

ʃ The market should be made transparent with the prompt dissemination of information to meet the expectations of investors of different parts of the country so that the involvement of the investors outside the valley could be enhanced.

ʃ Investments in the manufacturing sector should be enhanced. The government should think of the financial status of the firms in the manufacturing industries so as to make the appropriate policies and programs for raising the rate of return on investments.

ʃ Investors should be encouraged to invest in non-banking sectors. For this, the non-banking companies should think about their policy regarding the dividends on their stocks.

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