

# CHAPTER - I

## INTRODUCTION

### 1.1 Background of the Study

Capital Markets are the markets consisting long-term securities issued by the government or a corporation. Capital Market typically relates with financial assets which have life spans of greater than one year. Capital Market is a means through which scattered saving and investable resources are converted into actual investment. Capital market is one of the several factors that play a Prominent role in the economic development of the nation (Levine and Zervos, 1998: 1-3).The saving institutions such as banks, investment trusts or companies, specialized financial corporations and stock exchanges are some of the important constituents of capital market (Bolton and Thadden, 1998;5).The primary role of capital market is to allocate the economy's capital stock among various productive sectors (Fisher and Jorden, 2000:23). Capital invested in such sectors acts as *seed money* and generates more funds for further investments. No modern corporation of any size can function effectively without ready access to capital markets at the lowest possible cost (Bernstein, 1987: 54).

Nepalese Stock Market is very small as compared to other neighbor countries. Capital plays a vital role in the economic development of a country. Being a capital deficient country, Nepal has to make every endeavor to mobilize available capital effectively. Securities are financial assets. Securities markets are mechanism created to facilitate the exchange of financial assets. Therefore, the market exists in order to bring together the buyers and sellers of Securities. Capital market is the mechanism designed to facilitate the exchange of financial assets by bringing orders from buyers and sellers of securities

together. Stock market has been global phenomenon in the present world regardless of the size of any particular region.

Securities Market is place where buying and selling of securities take place in an organized way. The parties involved in Securities Market are investors, intermediaries and specialists. Security Market provides mobility of the scattered savings. Retail investors with limited capital fund could also participate in the industrial development process of the country through their investment in the securities. Investors who are willing to buy or sell securities quickly may be searching good offers or accepting poor offers with higher risk and higher return. Securities market is the major constituents of capital market. Although some analysts (Irwin Friend etc.) view securities market in developing countries as *gambling casinos* that have little positive impact on economic growth, recent evidence suggests that securities markets gives a big boost to economic development (Levine, 1996:7). Securities market is the pivot on which the economic development oscillates; it does mean that securities market is the foundation stone of any economic development. Securities market in developed countries has become an integral part of economy (Brennan, 1995: 11) and its role in developing countries is increasing day-by day. In securities market, the securities of listed companies are traded through organized brokerage firm (Douglas, 1991). It is, thus, a mechanism for bringing together buyers and sellers of financial assets in order to facilitate trading.

During the last one and half decade the financial sector in Nepal has grown significantly. It is said that despite a history of almost half a century of developmental efforts under different national plans, conscientious efforts to develop financial sector started quite late in Nepal. The history of capital market started since the period of Rana Prime Minister Juddha Shamsher. He set up a holding company namely Biratnagar Jute Mills under joint financing agreement with an Indian Jute processing industry in 1936(1933 B.S) as the first modern industry in the country. After that various mills of rice, cotton,

sugar and other were established to mobilize economy's capital for the industrial development. In 1937(1994 B.S), Nepal Bank Limited as commercial Bank was established. In the same year, the first individual act was promulgated which was a favorable step to promote capital market in Nepal. But Rana family did not like the participation of public in the ownership structure of industries and all the shares of company were gone to Rana families, the expansion of capital market to the desired level has been estimated. In 1950(2007B.S) democracy was established, the interim government were much busy in devising measures to recognize the sick industries and gave little attention to initiate the development of stock market. The process of stock market development in the country actually started in 1976 when the government established Securities Exchange Centre to provide and develop market for securities. However, visible impact on the development of financial sector was observed only when the government changed its restrictive policy and opened up hitherto closed financial sector to private sector and foreign participation in the establishment of banks. With the adoption of privatization and economic liberalization policy the process gets further impetus and the financial institution in Nepal grew at a faster pace especially in quantitative terms. Securities exchange centre was established with the objective of facilitating and promoting the growth of capital markets. Before its conversion into Nepal stock exchange, it was only capital market institution undertaking the job of brokering, underwriting, managing public issues, market making for government bonds and other financial services. It was converted in NEPSE i.e. Nepal Stock Exchange in 1993. The basic objective of NEPSE is to impart free marketability and liquidity to the government and corporate securities by facilitating transactions in its trading floor through members markets intermediaries.

Nepalese capital market was given proper structure in June 1993 with the establishment, SEBON as the market regulator. Since its establishment, SEBON has been concentrating its efforts on improving the legal and statutory

frameworks which are the bases for the healthy development of capital market. SEBON is the supreme body to regulate the Nepalese securities market. As a part of its continuous efforts to build a sound system, the securities Exchange Act, and 1983 was amended for the second time on Jan 30, 1997. This amendment paved the way for establishing SEBON as an apex regulatory body as it widened the horizon of SEBON by bringing Market intermediaries directly under its jurisdiction and also made it mandatory for the corporate bodies to report annually as well as semi annually regarding their performance. The main objective of SEBON is to promote and protect the interest of investors by regulating the securities market, to monitor and control the entire capital market, sale and distribution of securities and purchase, sale or exchange of securities. SEBON was established with the objective to render contribution to the development of capital markets by making securities transactions fair, healthy, efficient and responsible. Whereas, its main functions are to provide licenses to stock exchange and securities business person and to monitor the activities carried by NEPSE to know if they are in accordance with the laws or not. Despite this, Nepalese stock market is still underdeveloped and there is lot of shortcomings in Nepalese stock market. Hence, the present study is conducted on Nepalese stock market in order to find out its potential of growth, major problems and prospects by using secondary as well as primary data.

## **1.2 Statements of the Problems**

Development of capital market in general and stock market in particular is a must for a sound industrial development of the country. Capital market institutions help to mobilize the surplus unit into the deficit units for productive investments. As it mobilize the scattered resources and channels them in productive sector. It is an effective instrument of expanding productive capacities of the country. Due to the lack of information and poor knowledge investors are manipulated or exploited by the financial institutions or other market intermediaries such as extent that investing in common stock is

intolerably hazardous. Investor's attitude and perception plays a vital role in rational decision which is influenced by the knowledge and access to the data required for the analysis. Most of Nepalese investor invests their fund in single securities because of less knowledge about risk-return behaviors of the securities.

The development of stock market in Nepal is both challenging and difficult. The problem like lack of professionalism in brokers, independent buyers and sellers, well trained manpower; management delay of shares, rational investor exist from Nepalese stock market. Because of embryonic nature, Nepalese stock market is not effective enough to evaluate the price of stock. There are no private open investment companies (mutual fund) operating at present time. Therefore the government needs to create incentives for capital mobilization remove impediments to private sector development and provide basic legal regulatory reforms. The companies used different rules and regulation in stock market development. There is not consistency between Acts and Niyamabali. They are not matching each other .A special institute in corporate under a special charter governs accountancy profession. These institutes regularizes the profession also issues accounting standards and guidelines .All the members are required to follow mandatory, which discharge their duties. These practice helps to maintain a reasonable standardize performance by professional accountants.

Nepalese capital market is very small in comparison with other developed stock markets. There are a few numbers of brokers, limited number of listed companies, very few transactions and most importantly investors are unknown about the pros and cons of the stock market. The market is almost totally captured by individual investors who buy very little number of shares and therefore they do not bother analyzing the data and information before buying and selling stock. The variety of securities available in the market allows each

investor to select asset that suit his risk, preferences and beliefs. But there is lack of different types of securities in the stock market.

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

- ) Is growth rate of Nepalese stock market satisfactory?
- ) What are the problems of Nepalese stock market?
- ) What are the problems of Nepalese investors?
- ) What are the prospects of Nepalese stock market?
- ) What are the environmental conditions of Nepalese stock market?

### **1.3 Objective of the Study**

The general objective of the study is:

- ) To examine the growth of Nepalese stock market.
- ) To identify the existing problems and challenges faced by the Nepalese stock market.
- ) To analyze prospects of Nepalese stock market.

### **1.4 Significance of the Study**

Stock market recognizes the situation of economy. When stock market is booming the economy is good and when stock market is declining the economy is bad. Stock markets have direct relation with the economic growth.. Economic growths come with more earning capacity, opportunities to save and also the opportunity to invest. It must be noted that economic growth is, too a great extent, dependent on the industrialization in a country.

It represents the study to find out the problem, prospects and growth in the near future. What policies can be formulated, what regulatory acts are needed and necessity of amendments regarding the rules and regulation to develop it and make the market perfect functioning. The standard is one of the elements to stock market development. Financial statement should maintain accordingly which fulfill the requirement of related parties needed information.

This study will be useful to the university students who are curious to know about the current status of Nepalese stock market, its growth, issues and

challenges for the development of stock market. Similarly, the recommendations that this study intends to propose on the basis of its findings are expected to be useful for the policy makers associated with the development of capital markets.

### **1.5 Limitation of the Study**

It is not a comprehensive study. There are some limitations of the study. Lack of experiences, time, limited budget, up to date information are the main limitation of the study. Apart from this some more limitation are presented below:

- ) The subject of the study is only “Growth, Problems and Prospects of Nepalese Stock Market”.
- ) Up to 16 years period data are collected for the analysis purpose.
- ) The study covers only the past and present state of stock market in Nepal, hence does not make any prediction about the future.

### **1.6 Organization of the Study**

As discussed in the previous section, this study intends to find the Growth, problems, prospects of stock markets in Nepal. This study has been organized into 5 chapters. Each are devoted to some aspects of the study.

This study is divided into five main chapters. The first chapter Introduction consists of general background, statements of Problems of the study, and objectives of the study, Significance of the study, limitation of the study and organization of the study.

The second chapter Review of Literature deals with of the related studies. Therefore, this chapter includes the review of major journals, research work, and thesis etc along with conceptual framework.



The third chapter represents the Methodology adopted for the research design, sources and technique of data collection, population and sample.

The fourth chapter includes presentation and analysis of secondary and primary data. Major findings from both types of data have been also presented in the last portion of this chapter.

The fifth chapter elaborates summary of the study, conclusion and recommendations with bibliography and appendixes.

## **CHAPTER - II**

### **REVIEW OF LITERATURE**

In this chapter, an attempt is made to review some of the literatures concerning the stock market in Nepal. The chapter deals with the review of relating to the topic “A Study on Nepalese Stock Market in the light of its Growth, Problem and Prospects” in detail. Various books, journals articles and some previous research work related to this topic and many indirect topics are reviewed in the context of Nepalese stock market as well as international stock market.

#### **2.1 Conceptual Frame-work**

##### **2.1.1 Financial Market**

Financial market denotes the place or mechanisms where financial instruments are traded. Financial instruments denote also paper evidence, showing the exchange of instruments between concerned parties. A financial market is a place where firms and individuals enter into contracts to sell or buy specific products, such as stocks, bond on future contracts. This market provides a meeting place for buyers and sellers where price is determined.

Financial markets provide a forum in which suppliers of funds and demanders of loans and investments can transact business directly where as the loans and investments of institutions are made without the direct knowledge of suppliers of funds (savers), suppliers in the financial markets know where their funds are being lent or invested .The two key financial markets are the money market and the capital market .Transactions in short term debt instruments , or marketable securities (bonds and stocks ) are traded in the capital market (Gitman, 1988:30).

Financial market is the place where the financial instruments are traded. Financial instruments include share bond and debenture etc. The purpose of financial market in an economy is to allocate savings efficiently during the

period of time—a days, a week, a month, or a quarter to parties who use funds for investment in real assets or consumption (Van Horne, 2000: 448). It enables individuals to choose between current and future consumption. Second, it also provides the opportunity of interaction between buyers and sellers to determine the price of assets. Third it provides liquidity to investors. Fourth, it encourages management to comply with the existing rules and regulations. Therefore financial experts mentioned it as a brain of the entire economic system. The failure of the financial market, as a brain, obstructs the progress of whole economy. So, financial market from savers to users of funds to facilitate the efficient allocation and growth of financing and investment in financial assets transformation to generate income to savers and users (Sherestha and Bhandari, 2007:9).

A country's financial system may be bank dominated or market oriented. Each of this system has different mechanisms for handling holder's interest and addressing corporate control issues and agency problems. Though historically countries seem to follow one of these paths for development of its financial system, in recent years, some countries are developing their financial system through convergence between these two. Financial system helps in the payments of goods, services and productive inputs. Similarly, it helps to manage funds efficiently and use them. Financial system consists of financial institutions, financial markets and financial instruments.

Financial intermediaries (financial institution) are organization that issue financial claims against themselves and use the proceeds from this issuance to purchase primarily the financial assets of others. Financial claims simply represent the right hand side of balance sheet for any organization, so the key distinction between financial intermediaries and other types of organization involves what is on the left hand side of the balance sheet. Financial intermediaries provide an indirect method for corporation to acquire funds. Financial institutions are said to be the bridge between the savers and users.

They also collect scattered deposits and give loans to maximize their wealth. Financial institutions actively participate in the money market and the capital market, as both suppliers and demanders of funds. Financial intermediaries include, saving and loan associations, saving banks, credit unions, life insurance companies, mutual funds, pension funds etc. The financial system is an important element of modern economy

### **2.1.2 Securities Market**

The securities market is the place where large number of financial securities (shares, bonds, debentures etc) is traded according to the prescribed rules (Investors Guide, 1978:11). So far as the securities market is concerned, it is important constituent of capital market; it has wide term embracing the buyers and sellers of securities and all the agencies and institutions that assist the all sales and resale of corporate securities (Rugh, 1965: 50).

In Nepalese context, it is mandatory to register the portion of securities issued to the public with the security Board of Nepal (SEBON). Then the firms are eligible to issue the registered portion of securities through recognized bodies. The recognized bodies mean those who have received certificate from SEBON to act as issuing house and security promoter to get membership from security exchange market.

Security market exists in order to bring together buyer and sellers of securities, meaning that they are mechanisms created to facilitate the exchange assets. There are many ways in which security market can be distinguished. One is primary and secondary markets. Interestingly, the primary market itself can be subdivided into seasoned and unseasoned new issues. A seasoned new issue refers to the offering of an additional amount of an already existing security; whereas an unsecured new issue involves the initial offering of a security to the public. Unseasoned new equity issues are often referred to as initial public offerings, or IPOs. Another way of distinguishing between security markets

considers the life span of financial assets. Money markets typically involve financial assets that expire in one year or less; whereas capital market typically involves financial assets with spans of greater than one year (Sharpe, Alexander and Bailey, 2000: 9-10).

Securities market provides an effective way of raising money for commercial enterprises and at the same time provides an investment opportunity for individuals and institutions. Securities markets have both theoretical and practical perspectives. Securities markets provide value and significances to the financial assets. Practically, the activities of buying and selling securities on the security markets are extremely important for the allocation of capital within economics the securities market serves as a reliable guide to the performance of companies and thereby promoting efficiency.

Holders of stocks and bonds may decide to obtain cash for their investments by selling their securities to other investors. Similarly, others in the economy have cash to invest and are desirous of buying stocks and bonds. The problem is to bring together the order of prospective sellers and prospective buyers so that an exchange of securities for cash may take place. An efficient system whereby investors can convert their securities into cash quickly at or near the current market price makes investors more ready to put their savings into stocks and bonds (Bradley, 1663:303).

### **2.1.3 Stock Market**

Stock market is known as secondary market in the other side of market segment under capital market. It includes all transferable securities issued previously by corporate bodies; such securities are also traded in the stock exchange. Stock market does not include securities of private company as they are not capable of being dealt in on stock exchange and are not marketable securities due to the restrictions on transferability. In order to take the benefit from stock market the corporate bodies should have listed the security in the stock exchange.

Stock market covers activities pertaining to the dealing in securities, whether good or bad, for the liquidity and marketability. Only the securities of existing companies are tradable on the stock exchange irrespective of issuers corporate bodies or government (Vaidya, 2000: 72).

A stock market is a market for trading of publicly held company stock and associated financial instruments. Originally, stock markets were “open out cry”, where trading occurring on the floor of a stock exchange. Most modern stock trading is done in electronic exchanges where buying and selling occurs via online matching of order placed buyers and sellers (Manandhar 2063:2.8).

#### **2.1.4 Classification of Common Stock**

Common stock is often viewed as a homogeneous type of security. The majority of common stocks have similar voting, income, and liquidation rights. Nevertheless, despite the homogeneous nature of common stock, it is important to realize that the risk –return characteristics of stocks can vary significantly. Indeed, stocks are often classified on the basis of these characteristics (Cheney and Moses, 1995: 19).

##### **Blue –chips Stocks**

Stocks of very large, firmly established corporations, such as General Motors, IBM, and Xerox, are often referred to as blue chips. Many of these are included in 30 stocks that comprise the Dow Jones Industrial Average. Because of their dominant industry positions, strong balance sheets and size, these stocks are often viewed as conservative investments.

##### **Growth Stocks**

A common stock that is likely to experience above average price appreciation is known as growth stock. Accomplishing this may be a more difficult task than it first appears to be, however. First, the business may be successful increasing its market share or developing new markets.

### **Income Stocks**

Stocks that have a long – term record of stable cash dividends are often referred to as income stocks. For example, utilities are noted for their stable cash dividends .There stock prices, however, can be quite volatile depending on economic and market cycles.

### **Small Stocks**

There is no standard definition of how small a company must be to be a small stock. A NYSE traded company with a total capitalization of less than \$500 million may be considered small in relation to blue – chip stocks.

### **Treasury Stock**

Corporations have authorized, issued, outstanding and treasury stock. If a corporation decides to buy back its own stock, the acquired stock is called treasury stock that has been issued but is not outstanding. Consequently, it does not maintain voting rights and is not entitled to dividends.

## **2.1.5 Participants in Stock Market**

The major participants in Stock Market are:

### **i) Broker**

Various types of broker participate in stock market. A *stock broker* is a member of stock exchanges and *sub broker* is any person who acts on behalf of a stock broker as an agent or otherwise for assisting the investors in buying, selling or dealing in securities through such broker. Condition for granting of certificates to stock broker, the rules stipulates the registration is necessary for acting as broker or sub-broker. The conditions for grant of a certificate of registration to act as stock-broker are;

- a. He holds the membership of a stock exchange act.
- b. He shall abide by the rules, regulations and bye-laws of the stock exchange of which he is a member.
- c. He shall pay the amount of fees for registration;

A stock broker is expected to maintain high standards of integrity, promptitude and fairness in the conduct of his business. He is expected to exercise due to skill, diligence and comply with statutory requirements and not to indulge in manipulation and practice.

Almost all members act as *commission brokers*. The commission broker executes on the floor of the exchange buying and selling orders placed by his constituents to whom he renders contracts containing a charge for commission at rates not exceeding the official scale of brokerage. A brokerage firm or stockbroker accepts investors' orders to purchase and sell securities and is paid a commission for transmitting these orders to the appropriate exchange for execution. There are two broad types of brokerage firms-retail houses, which deal with individual investor, and wholesale houses, which deal with institutional investors. Some firms have both retail and wholesale customers. They include most of the well-known firms like Merrill Lynch, Pierce, Fanner and Smith Inco, Prudential Bache Securities Inc. Others, such as Salomon Brothers, however, accept only institutional investors as clients. As soon as an order is placed with a brokerage house it is relay by high speed lines to the exchange floor. They are the members of the exchange who actually see that customer orders get executed according to instructions.

The *floor brokers* are officially attached to other members. Floor brokers are also the member of the stock exchange and they assist commission brokers when there are too many orders following into the market for the commission brokers to handle alone. For their assistance, they receive part of the commission paid by the customers. Floor brokers are sometimes called two-dollar brokers because for a commission (which once was \$ 2 per order). They are ordinarily free-lance members of the exchange (Francis, 1992: 81).

## **ii) Floor Traders**

These members trade solely for themselves and are prohibited by exchange rules from handling public orders. They hope to make money by taking



advantage of perceived trading imbalances that result in temporary mis-pricings, thereby allowing them to “buy low and sell high”. These members are also known as registered competitive markets-makers, competitive traders or registered traders.

### **iii) Dealers**

A *dealer* buys securities at a price and accepts to sell them at a higher price. Dealers trade solely for themselves and are prohibited from handling public orders. Since dealers have access to the floor and can own securities in 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 add up to the liquidity of the securities.

The *odd- lot dealer* specializes in buying and selling in amount less than the prescribed trading units. He buys odd lots and makes them up into marketable trading units. He likewise sells odd lots obtained by buying or splitting up round lots. The odd- lot dealer doesn't rely on commission but earns profit on the differences between price at which he buys and sells.

The security dealers specialize in buying and selling securities, i.e. securities issued by government and public orders. They acts as jobber and is prepared to take risks inherent in the ready purchase and sale of securities to meet current requirement. The market is an OTC market and each purchase and sale has to be separately negotiated. The market, therefore, tends to be restricted (Bhalla, 1983: 9). Dealers have access on the floor and can own securities on their own name. They benefit from buying at low and selling at high price. The benefit of dealers to the market is that their buy and sells action added up liquidity of the securities.

### **ii) Market Makers**

Market makers, also known as specialists, facilitate the trading of securities by maintaining inventory in particular securities. They are similar to dealer 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 makers.

The market maker is any company or corporate body which deals in securities at the stock exchange in its own name or under its name on the basis of a pledge to provide liquidity to the securities, issued by HMG, as well as to the securities listed at the Stock Exchange by concluding necessary contracts with the concerned corporate bodies or to the securities of at least three corporate bodies and not to let to occur improper instability in the prices of such securities, shall be granted membership of securities market maker.

### **iii) Issue Manager**

Issue manager carry out the functions related to public issuance of securities on behalf of the issuing company. Issue managers are required to submit their annual reports including profit and loss account, balance sheet, cash flow statements and securities trading report to SEBON within four months of the expiry of the fiscal year. In this fiscal year eight issue managers have submitted their reports of the fiscal year 2008/09 to SEBON.

## **2.1.6 Types of Stock Market**

### **i) Primary Market**

Securities available for the first time are offered through the primary market. The issuer may be a brand new company or one that has been in business for many years. The securities offered might be a new type for the issuer or additional amounts of a security used frequently in the past. The key is that these securities absorb new funds for the offers of the issuer (Fischer and Jordan, 2000: 9). The primary markets are media through which new financial assets issued or generated. They are the media through the demanders and suppliers of today's funds, the creators and acceptors of financial claims meet. In these primary markets, financial assets are created and exchanged, satisfying in the part the financial needs of demanders and suppliers of today's fund. At

present context, it is the market for direct issuances of government securities. The primary market of country is dominated by the government securities due to the existence of insignificant new issues market for industrial securities.

## **ii) Secondary Market**

The secondary financial markets are that market where many outstanding assets are traded from old to new owners. The secondary market provides *liquidity* for financial assets making them more attractive. So, secondary market is a place where the securities once sold are purchased and repurchase to provide liquidity to the government securities. In Nepal, the secondary market is very thin because of limited distributors of the securities. NEPSE is established in order to promote the market used to support the market even involving itself buying and selling activities if necessary. Secondary market allows outstanding securities to be traded from old to new owner. The advantage of secondary market is to provide cash and investment opportunities to investor and to make certain assets more attractive to buyers and sellers. Secondary market comprises the stock exchange, the over-the-counter market.

Secondary market in simple, are markets in which outstanding securities are traded. It is the market that creates the price allow for liquidity. If secondary market did not exist, the investors would have no place to sell their assets. Without liquidity many people would not invest at all. The corporations whose securities are being traded are not involved in secondary market transactions and, thus, do not receive any funds from such a sale (Brigham, 2001: 115).

In conclusion, secondary market is a place where once securities purchased and sold to provide liquidity to the government securities and the market is operated by the securities exchange center. The trading of government securities is very thin because of limited distributors of the securities.

**iii) Third Market**

The Third market is an OTC market where the securities listed in the Organized Stock Exchange are also traded. More generally, the term “third market” now refers to the trading of any exchange listed security in the over the counter markets. The trading hours are not fixed to the third market like organized stock exchange and continue to trade securities even when trading is halted on an exchange. In the third market dealers provide only execution and record keeping services for their clients.

**iv) Fourth Market**

The fourth market also exists in the over the counter market and here trades occur directly among investors. In other words, in this type of market the buyer and seller deal directly with each other. This deal occurs in the exchange listed securities. Fourth market participants completely bypass normal dealer’s services. In this market, investors and investor securities are transacted. It is a communication network between block traders. The Fourth Market organizer collects only a small commission or an annual retainer for having to arrange block transactions. Thus, the costs of trading blocks are very small. Through the direct negotiation, more rapid execution and protection of anonymity, traders operating in the Fourth Market also expect to obtain better price. In the United States, some of these transactions are facilitated by an automated computer communication system called Instant, which provides quotations and execution automatically. A subscriber can enter a limit order in the computerized book where it can be seen by other subscribers who can, in turn, signal their desire to take it. Whenever two orders are matched, the system automatically records the transactions and sets up the paper work for its completion.

**v) Organized Securities Exchanges vs. over-the-counter (OTC) Market**

Organized securities exchanges are the physical locations where trading of securities is done under a set of rules and regulations. Company has to register

the share in this place. Without Registration Company share cannot be buy or sell. Company has to pay certain fee and renew share each year following certain rules and regulation. Investors usually purchase securities in the secondary market by calling securities brokers. In the secondary market investors buy and sell securities themselves, the issuer never gets any cash flow from the trades. Nepal stock exchange (NEPSE) is an example of organized stock exchange and this is the only stock exchange in Nepal. Similarly, the New York stock Exchange (NYSE), Tokyo stock Exchange, American Stock Exchange (AMEX), Bombay Stock Exchange (BSE) are the examples of organized stock exchanges. After an account has been opened, the broker relays the investor's order to a dealer that handles that security.

The organized security exchange are tangible physical entities. Each of the larger once occupied its own building, has specifically designated members, and has an elected governing body- its board of governors. Members are said to have "seats" on the exchange, although everybody stands up. These seats, which are bought and sold, give the holder the right to trade on the exchange (Weston & Brigham, 1997: 78).

The over the counter (OTC) exchange is not an organization but an intangible market for the purchasers and sellers of securities not listed by the organized exchanges. It is not a formal exchange like organized stock exchange. It neither requires membership for trading of securities nor listing of securities for trading, meaning that formal listing of securities are not necessary in the OTC market. A sophisticated telecommunication networks link active traders in this market. The prices at which securities are traded "over the counter" are determined by competitive bids and negotiation. The OTC, in addition to creating a resale market for outstanding securities, is a primary market in which new public issues are sold. Therefore, the OTC market competes with investment bankers and the organized exchanges because OTC dealers can operate in both the primary and secondary markets.

Securities with the following characteristics tend to be traded in the Over the counter market: securities of companies with a small capitalization, securities of companies which owned by a few holders; securities of government and their subdivision, and securities which are purchased in large books (such as government securities) by banks, life insurance companies, and other large investors, securities listed in an organized exchange etc.

### **2.1.7 Securities Board of Nepal**

Securities Board of Nepal was established on June 7, 1993 as an apex regulator of securities markets in Nepal. As per the Securities Act, 2006, the major objectives of SEBON are to regulate issue and trading of securities and market intermediaries, promote the market and protect investor's rights. The duties and responsibilities of SEBON are as follows.

- ) Register securities and approve prospects of public companies.
- ) Provide license to operate stock exchanges.
- ) Provide licensee to operate securities business.
- ) Give permission to operate collective investment schemes and investment funds.
- ) Draft regulations, issue directives and guidelines, and approve bylaws of stock exchanges.
- ) Supervise and monitor stock exchanges and securities business activities.
- ) Take enforcement measures to ensure market integrity.
- ) Review reporting of issuer and listed companies, and securities businesspersons.
- ) Conduct research study and awareness program's regarding securities market.
- ) Coordinate and corporate with other domestic as well as international regulators.
- ) Frame policies and programs relating to securities markets and advise the Government of Nepal.

The Governing Board of SEBON comprises of seven members representing various government and private sectors. The seven-member board includes a full time chairman appointed by Government of Nepal for the tenure of four years.

Other members of the Board are joint secretary from Ministry of finance, Joint secretary from Ministry of Law, Justice and Parliamentary Affairs, a representative from Nepal Rastra Bank (the central bank), a representative from Institute of Chartered Accountants of Nepal, a representative from Federation of Nepalese Chamber of Commerce and Industries, and a member appointed by the Government of Nepal amongst market experts.

SEBON, in its organizational structure, has two departments, six divisions and ten sections. Under the Corporate Finance and Administration Department, there are three divisions namely Corporate Finance and Reports Review Division, Accounts and Administration Division and HRD and Education Division. There are also three divisions under the Securities Market Regulation Department namely Legal and Enforcement Division, Market Regulation and Compliance Division and Market analysis and Planning Development Division. Presently, there is 42 staff (including chairman) in SEBON.

SEBON, in performing its responsibilities, is also taking opinions of experts from Accounting and Legal Professionals as and when required. Similarly, to make prospectuses of issuer companies more informative and reliable, SEBON has formed “Securities Registration and Issue Approval Committee” with representations from Nepal Rastra Bank and Insurance Board in this committee as and when required.

### **2.1.8 Nepal stock Exchange (NEPSE)**

The history of securities market began with the floatation of shares by Biratnagar Jute Mills Ltd. and Nepal Bank Ltd. in 1937. Introduction of the

company Act in 1951, the first issue of Government Bond in 1964 and the establishment of Securities Exchange centre Ltd in 1978 were other significant development resulting to capital markets. Securities Exchange was established with an objective of facilitating and promoting the growth of capital market institutions undertaking the job of brokering, underwriting, managing public issue, market making for government bonds and other financial services. His Majesty's Government, under the program initiated to reform capital market, converted Securities Exchange Centre in to Nepal Stock Exchange in 1993.

Nepal Stock Exchange, in short NEPSE, is a non-profit making organization, operating under Securities Exchange Act, 1983. The basic objectives of NEPSE is to impart free marketability and liquidity to the government and corporate securities by facilitating transactions in its trading floor through market intermediaries such as broker, market makers etc. NEPSE opened its trading floor on 13<sup>th</sup> January 1994 through licensed members. Government of Nepal Rastra Bank, Nepal Industrial Development Corporation and licensed Members are the shareholders of NEPSE.

### **Board of Directors**

The Board of Directors of NEPSE consists of nine directors in accordance with Securities Exchange Act, 1983; six directors are nominated by government of Nepal and different institutional investor. Two from the licensed members and the General Manager of the NEPSE is Ex-Officio Director of the Board.

### **Capital Structure**

The authorized capital of the exchange is Rs. 50 million. The issued capital is Rs.30 million of this, Rs 26.39 millions is subscribed by Government of Nepal, Nepal Rastra Bank, Nepal Industrial Development Corporation and licensed members.



## **Members**

Members of NEPSE are permitted to act as intermediaries in buying and selling of government bonds and listed corporate securities. At present, there are 28 member brokers and 3 market makers, who operate on the trading floor as per the securities Exchange Act, 1983, rules and bylaws of the exchange.

Besides these NEPSE has also licensed to dealer (primary market) and dealer (secondary Market). Dealer (primary market) operates as a manager to the issue and underwriter where as dealer (secondary Market) operates as a portfolio manager. Presently, NEPSE licensed to 11 dealers (primary market) and 4 dealers (secondary market).

## **Listing**

The listing fee and the annual fee to be paid by the listed company is based on the issued capital of the company.

## **Trading System**

NEPSE has adopted an “online system” for the trading purpose. It means transactions of securities are conducted using internet. The market makers quote their bid and offer price on their own website. Once the bid and offer price matches, contracts between the buying and selling brokers or between the brokers and market makers are concluded.

### **2.1.9 Stock Market Development**

Although the role of financial sector in the economic development of a nation remained controversial for sometime, recent theories in finance suggest that stock market do promote long- term growth (Duke, 1999; 36). Development of equity markets in any country requires political and economic stability and growth- oriented policies as pre-condition. At the second stage, equity prices rise and the investors gradually gain confidence in the equity market. They accept equity as an alternative to traditional bank deposits and government

securities. Equity markets gain more credibility and market liquidity increases. Investors long for rise in risk adjusted returns and demand a wide variety of securities to match their risk preferences. Rules and regulations are refined and the equity markets start functioning on the basis of self discipline, equity markets at this stage gradually get integrated to the international markets and attract foreign investors. At the third stage, equity markets become an integral part of the overall financial system. Investors get higher, less volatile returns and easily absorb new issues of stock and bonds. The volume of trading increases as the equity markets become more liquid and firms go for initial public offerings to replace their debts. At this stage a mechanism for risk transfer develops, creating markets for equity and currency hedging instruments such as derivatives and index products. At the final stage the equity markets get highly integrated with the global markets and the equity premiums match with the internationally competitive levels. Equity markets at his stage achieve stable growth and attain a mature state.

Despite its history of more than 25 years with respect to the above – mentioned observation, the equity market in Nepal has barely entered the first stage of development. Due to current political and economic instability, absence of growth oriented policies and weak regulatory framework of stock market has failed to gain investors' confidence. Unavailability of timely information and weak supervision and monitoring has made the stock market highly risky for general investors. Investors have not yet accepted investment in stock as an alternative to bank deposits and government securities except in the case of stock of some commercial banks (K.C. and Snowden, 1997: 1083).

By encouraging and dissemination of information, stock markets reduce cost of mobilizing savings and facilitate investments. Well developed stock markets enhance efficiency of market for corporate control by mitigating the agency problems between the stockowners and managers. In countries where stock

discipline is effective, firms tend to be more productive, thereby creating more wealth per unit of money invested (Diamond and Verrecchia, 1982: 275).

Stock markets help expansion of economic activity by providing liquidity to financial assets traded in them. Investments in real assets require long-term commitment of capital, however, investors are reluctant to commit their investment less risky because they allow savers to buy and sell financial assets they hold cheaply and quickly and restructure their portfolios any time according to their risk-return preferences. At the same time firms enjoy permanent access to long-term capital through equity issues. By making assets less risky and providing easy access to permanent source of capital, liquid stock markets improve allocation of resources, boost investment and enhance long-term economic growth by encouraging investor myopia. It is argued that such stock markets may weaken investor's commitment to exert corporate control because they prefer to sell the stocks of the misgoverned companies rather than to monitor and force managers to improve their performance. However, empirical studies suggest that greater stock market liquidity boosts and in many cases precede economic growth.

#### **2.1.10 Regulation of Security Markets**

Securities market should be strictly regulated to stop the malpractices and to develop efficiently. Securities Board (SEBON) of Nepal is the supreme body to regulate the Nepalese securities markets. It was established on 26 May, 1993 under the provision of the securities Exchange Act, 1993. The objective of the board is to promote and protect the interest of investors by regulating the securities markets, Not only these, to regulate, monitor, direct and coordinate the entire capital market is also the objective of the SEBON. SEBON works under the Ministry of Finance (MOF). SEBON regulates both primary and secondary markets. To regulate primary markets different acts and laws have been passed. The public issue activities through the primary market are regulated by the securities Exchange Act, 1983, the regulation and guidelines

are made under the act as well as the Company Act, 1997. The related regulations and guidelines are Securities Exchange Regulation 1993, Securities Registration and Issue Approval Guidelines, 2002 and securities Allotment Guidelines, 1997. Similarly, to regulate the public issue it has made it mandatory to take services of an issue manager by the issuing companies. To regulate secondary markets as well as the members, different Acts like Member of stock Exchange and Transaction Byelaws 1998, and securities Listing Byelaws 1996 have been passed, SEBO also monitors whether the activities carried out by the NEPSE are in accordance with the above laws or not. Similarly, SEBO regulates all the members of the secondary as well as primary markets like issue managers, stock brokers, dealers, market makers and corporations.

### **2.1.11 Major Regulating Agencies**

Three government agencies, viz. Securities Board, Company Registrar's Office and Nepal Rastra Bank are involved in approving and registration of public issues. Though Securities Board is the only regulatory body in securities market to supervise and regulate the overall functioning of the market, the functions performed by other two agencies seems to of duplication of works. Here, how all three bodies work in approving and registering the public issue are elaborated.

#### **i) Securities Board**

Securities Board is empowered by Securities Exchange Act 2040 for the development of capital market, protection of Investor's interest, approval of stock exchange, regulation of market intermediaries, secondary and primary markets, mutual funds and conducting investment awareness programs for various interest groups. When prospectus is submitted for the registration purpose, the securities board betting and if disclosures in the prospectus are found then Board registers the securities to be issued in the public and grants permission on it.

**ii) Nepal Rastra Bank**

Nepal Rastra Bank, the central bank, approves prospectus when banks and finance companies propose public issue. It also gives permission to issue debentures in the public along with the approval on interest rate on debentures and bonds. Under NRB directive bank and finance companies are required to issue shares equivalent at least 30 and 40 percent in both situations if they have foreign joint venture stake.

**iii) Company Registrar's Office**

The company Registrar's office is the only agency where companies are registered. It monitors the operations of the companies and makes arrangements for winding up of the companies when required. Approval on the prospectus is granted by the company Registrar's office only. Before granting an approval it obtains the advices/opinion from the securities board and for banking and finance companies opinions/advices on the prospectus is taken from Nepal Rastra Bank too.

**iv) Nepal Stock Exchange**

While issuing securities to the general public consent should be obtained from the NEPSE. For this the issuing companies and issue managers are required to submit the prospectus.

**v) Insurance Board**

When a public issue is made by an insurance company, the insurance board also performs the vetting of prospectus as it is done by Nepal Rastra Bank.

**vii) Concerned Ministers of Government**

The companies which are incorporated by special acts are required to get their prospectus approved from concerned ministers. For example, companies such as Nepal Investment Trust, Rastriya Beema Sansthan, Nepal Industrial Development Corporation are under the preview of the Ministry of Industry

and Ministry of finance. Thus the prospectus of these companies is required to be approved by the ministry of industry and ministry of Finance instead of the company registrar's office.

## **2.2 Review of Articles and Journals**

No specific research studies have been available regarding the growth of stock market, its problems and potentials and its impact on economic growth in Nepalese context .However, some articles and journals which are related to stock market are consulted and reviewed.

The 1980s were an easy decade for fund managers. Both stock market and commercial property investment provide high return by historical criteria. Whether or not fund managers added value, stock investors obtained high return. The easy market condition of the 1980s did not persist into 1990 and investment returns in real terms during the 1990s are unlikely to match those of the 1980s. Fund managers have some protection because of tax advantage for investors of investing through institution rather than by direct companies. However, some aspects of the operation of the stock market are seen inefficient and called for comments. These inefficient may, in part, be a hangover from the regime of fixed commission when broker competed by providing fund managers with data and company analysis of information about the companies is that their primary motivation is to get clients to buy or sell shares, and this might introduce a bias towards dwelling on the strong or the weak points in a company's record (Pratten, 1994: 182). Stock market and their subsets, emerging growth stock, are well managed companies operating in industries where earning and dividend are expected to grow faster than inflation and overall economy. They are expected to maintain their exceptional growth momentum through economic retractions as well as during economic prosperity. Growth stocks are not located in the traditional smokestack industries but in new and upcoming fields, such as computer, telecommunications, healthcare and biotechnology. Major characteristics of

growth stock include higher price/ earning ratios than the market average, substantial potential for above average long-term price appreciation, price volatility and correlation of capital to fuel growth, therefore little or no dividend pay-out in the early years (Maturi, 1994: 138).

Mahat (1981) in *Capital Market, Financial Flows and Industrial Finance in Nepal* has said that there is absence of secondary market to ensure liquidity to the securities on demand. Any attempt to stimulate investment in industrial sources would naturally depend on the extent to which the securities are salable in the market. Only the existence of stock exchange can enable the security holders to sell their securities for cash and purchase alternate securities if they wish. In Nepal, in the absence of such a stock market, and industry security is an illiquid form of asset, even more illiquid than the real estate for all practical purpose.

Pradhan (1993) has conducted a study on *Stock Market Behavior in a small Capital Market: A case of Nepal* by collecting the data of 17 enterprises from 1986-1990. He has applied Market Equity, Market value to Book Value, Price Earning and Dividend as technical tools to analysis of data. His findings indicate that larger stocks have larger price-earning ratios, larger ratios of market value to book value of equity, lower liquidity, lower profitability, and smaller dividends. Price – earning ratios and dividend ratios are more variable for smaller stocks whereas market value to book value of equity is more variable for larger stocks. Larger stocks also have higher leverage, lower assets turnover, and lower interest coverage but these are more variable for smaller stocks than for larger stocks. Stocks with larger market value to book value of equity have larger price-earning ratios, and lower dividends. These stocks also have lower liquidity, higher leverage, lower earnings, lower turnover, and lower coverage.

Capital market is a crucial element in the national economy. Its role in reinvigorating and boosting the economic activity in the country is significant. The strategic plan released by securities board can, to a great extent, energize the investors, dealers by increasing investor interest in it. Securities market experiences both boom and bust soon after the beginning of securities trading through brokers' member in the stock exchange floor. Though the market started to function quickly boosting the price of share to an unexpected level, it could not sustained.

As an apex regulatory body for the Nepalese Securities Market, The securities board has adopted following set of strategies policies to handle the strategic issues that are inhibiting the growth and development of the market. This policy consists of improvement in the statutory and regulating framework of the capital market, development of widely participated capital market and improvement in the securities board's institutional capacity. SEBON has also made some improvements in the statutory and regulatory framework of the capital market. Such improvements contribute to the development of capital market in the following ways:

- ) Bring clear demarcation in the role and responsibilities borne by the securities board another regulatory agencies i.e. stock exchange, NRB, ORC etc.
- ) Reduce the duplication in the role and responsibilities of Board and other regulatory agencies.
- ) Show the ways of coordination between the services Board and other regulatory agencies.
- ) Establish securities board as a central market regulator and rest in with wider investigation and enforcement power.
- ) Promote the development of 'full-services' securities house and gives focused attentions for the establishment and up grading of necessary legislative infrastructure to address on going needs.



Nepalese capital market offers a wide range of financial services and instruments. It also has to provide the opportunity for a large number of investors to participate directly or through mutual savings schemes. While implementing this policy the securities board advises the government regarding the development of secondary market for government securities and the opening of foreign portfolio investment, coordinates with NRB to formulate prudential standards for the primary issue as well as secondary trading of government bonds and studies the possibility of introducing as over the counter exchange system and brings in the concept of introducing broker in order to facilitate easy entry and exist process for the benefit of investors.

Koirala and Bajracharya (2004) published an article "*Nepalese Capital Market :Issues and Challenges*". In the article, they have focused that establishment of the Nepal Stock Exchange (NEPSE) market opened an avenue to investors, both large and small, to invest in the enterprise sector and participate in the Secondary market. Despite apprehensions of many, the secondary market proved to be successful, with both the entrepreneurs and the investors showing earnest acceptance and participation in the investors showing earnest acceptance and participation in the process. However the performance of stock exchange during the latter years given only a mixed result. The enthusiasm did not last long as, after 2000/01, both size and trend began to shrink. The NEPSE index came down to shrink. The NEPSE index came down to 204 in 2002/03 from a peak of 360.70 in 1999/00 but then after it rises till 2007/08 with 963.36 points and decreased in 2008/09 with 749.1 points. The transaction volume to about Rs 21681.14 million in 2008/09 compared to Rs 2344 million in 2000/01 .This scenario despite increasing number of listed securities and scrip's is not favorable situation. Generally, the problem is attributed to politico –economic situation.

No doubt, it is true to a large extent but the problem is not confined to the present situation alone. The management of the companies and the attitude of

the broad of directors and intermediaries are to blame a lot. The actors of financial markets are loosely tied together from legal provisions, which are not effectively implemented. As the financial institutions predominate the market, it has not been able to diversify. Increasing problems noted with the corporate transparency and disclosure has seriously dented the Nepalese capital market. The Board mainly acts as a superfluous body trying to fulfill formalities rather than seriously attending to corporate governance. The result has been poor security to investors, particularly minority shareholders, who are not fully aware of the risk and return considerations. Hence to make the stock exchange a vehicle of growth, initiatives must be taken to protect investors, improve corporate governance and make the companies operate in a conducive and transparent manner.

Many investors in the Nepalese stock market do not know that they are being cheated by brokers who use a relatively unknown technique called “Matching”. The investors cheated by this method are normally those who occasionally buy or sell shares, not the regular ones. Matching and Slitting are the most prevalent mode of securities transaction in Nepal. According to the Securities Board of Nepal, the regulators of the country’s stock market about 65 percent of the total transactions in the NEPSE are executed through matching (Bhattarai, 2005: 67).

Sherstha (2007) conducted a study of “*NRB Monetary Policy and Stock Market Impacts*”. He has found that the lesson learned from New Monetary Policy Announcement is that it should be a long term policy and should not interface in the price sensitive capital market phenomena determined from the free play of the market forces.

Kafle (2007) published an article in SEBON journal entitled “*Building a Dynamic Capital Market*”. He has highlighted the important reform initiatives and some critical aspects of capital market development in Nepal. The vision

of new Nepal has to have an important place for dynamic capital market. Nepalese financial system is characterized by small but growing capital market. During the past 16 years of its operation, securities market has witnessed three market phases of ups and downs.

The market lacks sectoral diversification of performing listed companies, access to secondary trading issuer and market is not sufficient, capacity of regulator, exchange and the players is limited, the market is featured by active individual investors and the institutional investors are conspicuously absent. The market infrastructures supporting the trading, clearing and settlement are not sufficient. Thus the effort to build a dynamic market is going to be an ardent task requiring a lot of commitment and efforts of the government, regulator, market players and the investors.

He concluded that the government sector involvement in the market operation should be shifted to benefit from private sector efficiency and competition, and its focus should be towards strengthening the market regulator and in building market infrastructure.

### **2.3 Review of Thesis**

There are various masters' thesis prepared by various researchers in the past year. Among them, some of these are reviewed here for analysis of literatures.

Bhattarai (1990) has carried out on "*Share Market in Nepal*". In which, he emphasized the historical background and the analysis of various financial variables affecting the smooth operation of share market. This study was mainly based on secondary data obtained from various sources. He has applied both financial and statistical tools in the study. He found that out of 12 sample companies 2 companies were useful to cross over the average price-earning ratio, as a result, market price of shares were highly skewed. Moreover, there was mismatch between calculated and quoted price. However, he concluded

that the involvement of more and more institutions as well as individual investors in capital market through broker's network raised the transaction volume. Rumors spread by brokers and create genuine speculation. Fair plays of bulls and bears make market equilibrium resulting price stabilization speculation on the trading of shares is encouraged. Thus, the market starts to walk randomly reflecting true value of shares. Investors are facilitated by providing alternatives to make diversified portfolio.

Bhatta (1996) in his thesis paper "*Assessment of the performance of listed companies in Nepal*" concludes that a highly significant positive correlation ship has been addresses between risk and return chapter of the company. Investors expect higher return form that stock, which associates higher risk. Nepalese capital market is not efficient one. So the stock price does not contain all the information relating to market and company itself. Neither investors analyze the overall relevant information of the stocks nor does the member of stock exchange try to disseminate the information. So the market return and risk both may not show high priced stocks. In the addition, Bhatta further addressed that Investors of Nepal have not yet practiced to invest in portfolio of securities. An analysis of the two securities portfolio shows that the risk can be totally minimizes if the correlation is perfectly negative. In this situation, the risk can totally be diversified, but when there is perfectly positive correlation ship between the returns of the two securities the risk is not diversified.

To some extend he focused in the analysis of risk and return in common stock investment. But due to many other aspects to analysis investor cannot easily assess the results. Indeed, study did not focus the viewpoint of investors rather it concentrates the companies and stock market. However, this study also explores some dimension for further research in his topic.

Khatiwada (1996) in his thesis paper "*A study on securities Investment in Nepal*" concludes that; leaving some exceptional cases aside, almost all the

companies experienced their market price going down by less than fifty percent in 1995. Even the banking group could not spare the share price going down more specifically, the year 1995, was a disheartening period for the stock price. It is because, almost all the companies share price during the year were down even in some cases below the face value. Through the study conducted by Katiwada did not focus the analysis of individual security and the viewpoint of investors, it explores some dimension to further research in this aspect.

Bhatta's (1997) study on "*Dynamic of Stock Market in Nepal*" revealed that resource mobilization has a vital role in the developing economy like Nepal. The development of Stock Market in Nepal is a must for the resource mobilization. There are various problems of Nepalese Stock market, which have checked the resource mobilization in the economy. In his research work, he set the following objectives:

- ) To analyze the trend of Nepalese stock market.
- ) To diagnoses and compares the sectoral financial status of the stock in Nepalese stock market. To analyze the market share prices of the Nepalese stock market.
- ) To find out the impact of the secondary or primary market and vice versa.

He made the following recommendations:

- ) The government should make not only policies for the capital market development but also implement these policies appropriately.
- ) Investment in corporate sector should be encouraged and their share should be listed in the stock exchange.
- ) The regulatory authorities of the stock market should create environments to rise the trading of share in the stock exchange.
- ) The government should make appropriate policies and programs for the enhancement of the entrepreneurship development in the Nepalese economy.

In conclusion, he tried to show that although it has become late to take steps to overcome such problems of the Nepalese stock market in order to make it active and supportive; the stock market has a good prospect for the resource mobilization to finance the productive enterprises in the Nepalese economy.

Sherestha (2000) had studied on “*Growth and Prospect of Stock Market in Nepal*”. He tried to show the role of the capital market in Nepal which has been increasing as to mobilize the saving of the nations and canalized them in to productive activities. But, the major problems in the process of development are to increase the level of saving and canalize those savings into investment, which leads to economic growth. Capital market is playing a crucial role in the process of growth .In this way, the important of capital market arises as to proper allocation of accumulated savings to various economies. Objectives of the study were to identify the legal obstacles in the stock market development and to analyze existing transaction system.

After the analysis of the study, He made the following recommendations:

- ) The provision of Annual General Meeting (AGM) should be with in four months from the completion of each financial year.
- ) Financial statement and annual reports of the company’s should be presented to authority within the three months from the completion of each financial year.
- ) Stock market translation is depending on the demand and supply of security for sell or buy.
- ) Market moves are the important indirect factor for the stock market translations. GDP, interest rate, rate of inflation, foreign exchange rate and commodity price are the main movers of stock market. They affect the share price of the companies in the market.
- ) Government and investors should be conscious in these factors whereas so many changes will be in these movers. Government should be more concerned in decreasing of GDP, and increasing of interest rate, rate of

inflation and commodity price. Government should give attention to the foreign exchange rate, which also change frequently in Nepalese capital market.

- J) Information is the one of the main elements of stock market development. Every stock market transactions are depending in the information provided by the companies. Therefore security board and stock exchange limited should be in coordination in the information provided by the companies for stock market development.

Pant (2000) has analyzed in her thesis “*Current Status and Problems of Stock Market in Nepal*” with an objective to analysis the problems and trends of present state of Nepal Stock Market and suggest measures for the improvement of stock market. The researcher mostly used secondary data collected from books; company Act, Official records of the NEPSE, Securities listings By-laws, Act, Government publication etc. She found in her study that the development of stock market primarily depends on the government policies and program and their proper implementation. So, government should develop an appropriate policy framework to increase the demand for supply of securities. She also found that there is a lack of investor’s confidence in the stock market since many listed companies do not trade on a regular basis or hold AGM and provide disclosure information to the investors on a timely basis. Beside this, there is a general lack of investor’s awareness about the listed companies.

Jeevan, Puspa and Arjun (2000) in their research work, “*Investment Management in Stock Market*” concludes that individual Nepalese savers have extremely limited opportunities for investing their long- term savings. To secure maximum returns, these investors should have opportunity to invest into long-term corporate equities rather than state of the stock market. Both individual and institution are putting for more of their savings into bank deposits and fixed interest, government securities than they would if the market

were working properly. Thus, long-term saving that should be invested in the stock market is going into short term investment.

They made conclusion in the same study that the development of primary stock market in Nepal so far cannot be considered satisfactory. This is evident from the fact and figure available in the primary stock market performance during the last nine years. But there is enough long-term liquidity in the market; investors are in search for investment opportunity in the equity of corporate bodies.

Khanal (2003) has prepared the thesis on “*Growth, Problems and Prospects of Nepalese Stock Market*”. The main objective of the study were to examine the investors’ awareness, to examine the stock broker’s and other related institution performance, to analyze sector wise financial performance of NEPSE, and to observe the coordination among SEBON, NEPSE and Rastra Bank.

In this study, Khanal concluded that the development of stock market in Nepal so far can not be considered satisfactory. This is evident from the facts and figures available in the stock market performance. But there is enough long term liquidity in the market. Again he added that the stock market and economic activity move in similar direction. They influence each other. Nepal Stock Exchange is the only one institution in the country to regulate and control the financial system of a country. The official stock market in Nepal, NEPSE is ten years old. It means it is in infant stage thus equity market and related institutions are still in their infancy stage.

Paudel (2005) entitled “*Stock Price Behavior of Commercial Banks in NEPSE*” with the objective to examine monthly closing price of 6 listed commercial banks during the period of three consecutive years from 2002 to 2004. The researcher used correlation coefficient, regression analysis, and run test and auto correlation. He found in his study that successive price changes were



correlated with previous price series. He also found that most of the stocks did not follow random walk hypothesis. The present stock prices were dependent to the historical prices. The EPS was the most affecting factor for the price change of the stock. Most of the investors wanted to invest in the shares of commercial banks because the fluctuation in NEPSE index was due to the transaction of commercial bank shares. There were serious limitations in the study. Data used in this study, monthly closing price of stocks not enough to predict the behavior of share prices.

Shrestha (2005) has carried out a study on “*Growth of Stock Market in Nepal*” with the objectives to trace out the current situation of primary market from the year 1994/95 to 2004/05. The researcher used standard deviation, percentage, multiple bar diagram to trace out the picture of stock market in Nepal. Her study was based on secondary data with the large samples of listed companies from different sectors. The researcher applied historical data and statistical tools in her study. Thus, she concluded that there is significant development in various stock market indicators in stock market. The laws and policies regarding market are not very clear. There is not enough foreign investment in the stock market.

## **CHAPTER - III**

### **RESEARCH METHODOLOGY**

#### **3.1 Introduction**

Research means to search or study about a phenomenon. Generally research is an effort to search new fact, knowledge and principle in scientific ways. Therefore this chapter highlights the research methodology used for the study of “A Study on Nepalese Stock Market in the Light of its Growth, Problem and Prospects”. In this regard, this chapter explains not only talk of the research methods but also consider the logic behind the methods, which are used in the context of our research. This chapter consists of the research design, population, sampling procedure and sources and analysis of data.

#### **3.2 Research Design**

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

This research is based on secondary data and primary data analysis. Hence, the historical and descriptive research design has been used to conduct the study on focus of growth, problems and prospects of Nepalese stock market It deals with the stock market on the basis of available information.

#### **3.3 Population and Sample**

The analysis of stock market, its growth, problems and prospects depends on the number of company listed in the Nepal Stock Exchange and major economic indicator (GDP, Inflation, Turnover etc) are taken as total population. Moreover, the companies that are in existence and doing share

transactions in NEPSE and the factor that affects the present economic growth are considered as the convenient sample of the study.

### **3.4 Sources of Data**

The required data have been collected from the various sources; but mainly from the annual reports of securities exchange board, Nepal covering a period of 1993/94 to 2008/09. The main place of data was the central office of Nepal Stock Exchange (NEPSE), Securities Boards office, Kathmandu and Economic Survey published by Ministry of Finance. The main source of data is annual report of the SEBON. Besides annual report, various bulletins available and useful to the study are also taken into consideration. The research is mainly based on the secondary data.

#### **Primary Data**

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

#### **Secondary Data**

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

### **3.5 Data Collection Technique**

The research contains of both primary as well as secondary data. Since the nature of these two data is different, the data collection procedure also varies.

To collect the secondary data, published materials are viewed in various spots such as books by different authors, unpublished thesis reports, journals, Internet web sites, online library, AGM reports of listed companies, NEPSE, SEBON etc. To collect these secondary data, the researchers visited campus library, SEBON library. On the other hand, the primary data collected through scheduled questionnaire.

### **3.6 Data Processing**

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

### **3.7 Analysis of Data**

Analysis is the careful study of available facts so that one can understand and draw conclusion from them on the basis of established principles and sound logic. This study is mostly based on the analysis of secondary and primary data with the help of different statistical tools like Diagrammatic presentation and mean. The empirical result has been extracted in this study by using annual data of listed companies from 1993/94 to 2008/09.

### **3.8 Data Analysis Variables**

#### **Gross Domestic Product (GDP)**

The GDP is the total rupee value of all the final goods and services produced and consumed in country during the year. It is the broadest quantifiable

measure of economic activity in the country. Change in GDP measures the increase or decrease in the nation's capacity to produce goods and services.

The rate of growth of GDP influences the investor's perceptions of the country's economic future. A sustainable high rate of growth signals a long-term bull market in share and property values. It also points to higher price earning multiplier to the stock exchange.

### **Issue Approval**

The issuing company should register the securities in SEBON and get issue approval before going to the public. During the process, SEBON reviews the prospectus and other relevant documents submitted by the existing rules and regulations. In the process, SEBON has also been taking the comments of the experts as and when it deems necessary.

### **Public Issue**

Securities Registration and Issue Approval Guidelines has made provision that a company must float its share to the public within two months from the date of getting approval from SEBON. During the fiscal year 2008/09, SEBON registered Rs.2509.76 million worth of securities of 11 companies comprising four commercial banks, three development banks, two finance companies, and two hydropower companies and approved their prospectuses for public issue. SEBON, in the fiscal year 2008/09, approved the prospectuses of two commercial banks amounting to Rs.750.0 million for the debenture issue.

### **Issue Manager**

Issue manager carry out the functions related to public issuance of securities on behalf of the issuing company. Issue managers are required to submit their annual reports including profit and loss account, balance sheet, cash flow statements and securities trading report to SEBON within four months of the expiry of the fiscal year. In this fiscal year eight issue managers have submitted

their reports of the fiscal year 2007/08 to SEBON. In this fiscal year, out of nine issue managers, Five were involved in the issue management activities.

### **Stock Broker**

Stock Brokers are required to submit their annual reports including profit and loss account, balance sheet, cash flow statements and securities trading report to SEBON within four months of the expiry of the fiscal year. In this fiscal year 22 stock brokers submitted their reports of the fiscal year 2007/08 to SEBON.

### **Paid-up Value, Turnover and Market Capitalization**

The total paid-up value of the listed securities by the end of 2008/09 fiscal year reached Rs.61140 million. The paid-up value in the last fiscal year was Rs.29465 million. By the end of 2008/09 fiscal year, the market capitalization of the listed securities reached Rs.512939.07 million. In the last fiscal year, the capitalization was Rs 366247.5 million. By the end of this 2008/09 fiscal year, the percentage contribution of market capitalization on nominal GDP is estimated to be 53.43.

## **3.9 Tools of Data Analysis**

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

### **3.9.1 Arithmetic Mean**

An arithmetic mean is the value, which represents the group of values and gives an idea about the concentration of values in the central part of the distribution. An average gives us a point, which is most representative of the data. It depicts the characteristic of the whole group. The value of arithmetic

mean lies in between the two extreme observations of the entire data. It is an envoy of the mass of homogeneous data. An arithmetic mean of a set of observations is defined as the ratio of the sum of all the observations to the total number of observation.

The Value of the AM is obtained by adding together all the items and by dividing this total by the number of items.

Mathematically,

Arithmetic Mean (AM) is given by,

$$\bar{X} = \frac{\sum X}{N}$$

Where,  $\bar{X}$  = Arithmetic Mean

$\sum X$  = Sum of all the values of the variable X.

n= Number of observations

### **3.9.2 Diagrams and Graphs**

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

## **CHAPTER IV**

### **DATA PRESENTATION AND ANALYSIS**

In this chapter, the relevant and available data and information from Nepal stock exchange (NEPSE), Security Board of Nepal (SEBON) and different articles are presented, analyzed and interpreted to find out the growth, problems and prospects of stock market in Nepal. Data presentation and interpretation is the important part of a research work which analyze the data and information using various tools and techniques to get the best results.

The data are collected through primary sources and secondary sources. Such collected data are presented in systematic formats and analyzed using different tools and techniques. The analysis of questionnaire is also done in this chapter. This chapter has been divided into two parts, the first part deals the presentation and analysis of secondary data and second part is concerned with presentation and analysis of primary data.

#### **4.1 Presentation and Analysis of Secondary Data**

This section deals with the presentation and analysis of the collected secondary data. This part of the chapter reveals the growth of Nepalese stock market in terms of amount of issue approval, number of issue approval, and number of listed companies, paid –up value, annual turnover, market capitalization and NEPSE Index etc with different years.

##### **4.1.1 Analysis of Amount of Issue Approval and Number of Issue Approval**

The issuing company should register the securities in SEBON and get issue approval before going to the public. During the process, SEBON reviews the prospects and other relevant documents submitted by the existing rules and regulations. In the process, SEBON has also been taking the comments of the experts as and when it deems necessary.



**Table 4.1**  
**Amount of Issue Approval and Number of Issue Approval**  
**(From fiscal Year 1993/94 to 2008/09)**

| <b>Fiscal Year</b> | <b>Amount of Issue approval (Rs in million )</b> | <b>Percentage of Growth</b> | <b>No of issue Approval</b> | <b>Percentage of Growth</b> |
|--------------------|--|-----------------------------|-----------------------------|-----------------------------|
| 1993/94            | 244.4  | –                           | 16                          | –                           |
| 1994/95            | 174  | -28.81 %                    | 10                          | -37.50 %                    |
| 1995/96            | 293.7  | 68.79                       | 12                          | 20                          |
| 1996/97            | 322.2  | 9.7                         | 5                           | -58.33                      |
| 1997/98            | 462.4  | 43.51                       | 12                          | 140                         |
| 1998/99            | 258  | -44.2                       | 5                           | -58.33                      |
| 1999/00            | 326.9  | 26.71                       | 6                           | 20                          |
| 2000/01            | 410.5  | 25.57                       | 9                           | 50                          |
| 2001/02            | 1441.3   | 251.11                      | 12                          | 33.33                       |
| 2002/03            | 556.3  | -61.40                      | 18                          | 50                          |
| 2003/04            | 1027.5   | 84.70                       | 14                          | -22.22                      |
| 2004/05            | 1626.8   | 58.33                       | 14                          | 0                           |
| 2005/06            | 2443.3   | 50.19                       | 29                          | 107                         |
| 2006/07            | 2295.50  | -6.05                       | 34                          | 14.70                       |
| 2007/08            | 10668.20   | 364.74                      | 64                          | 88.23                       |
| 2008/09            | 16828.51   | 57.74                       | 64                          | 0                           |

*Source: Annual Report, SEBON, 2008/09*

**Figure 4.1**  
**Trends of Amount of Issue Approval**

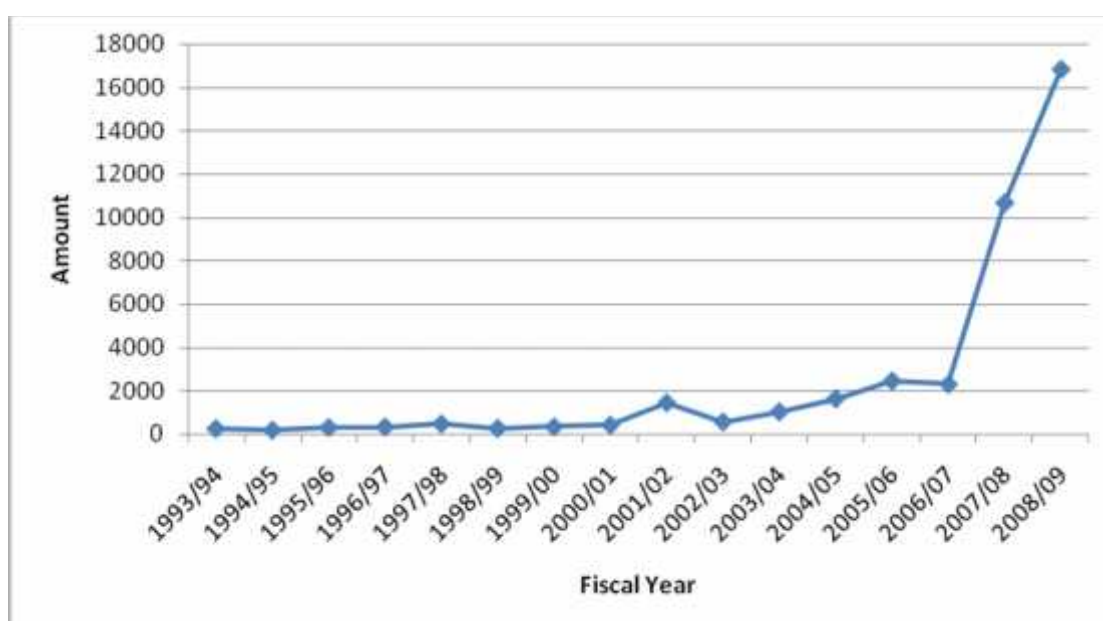
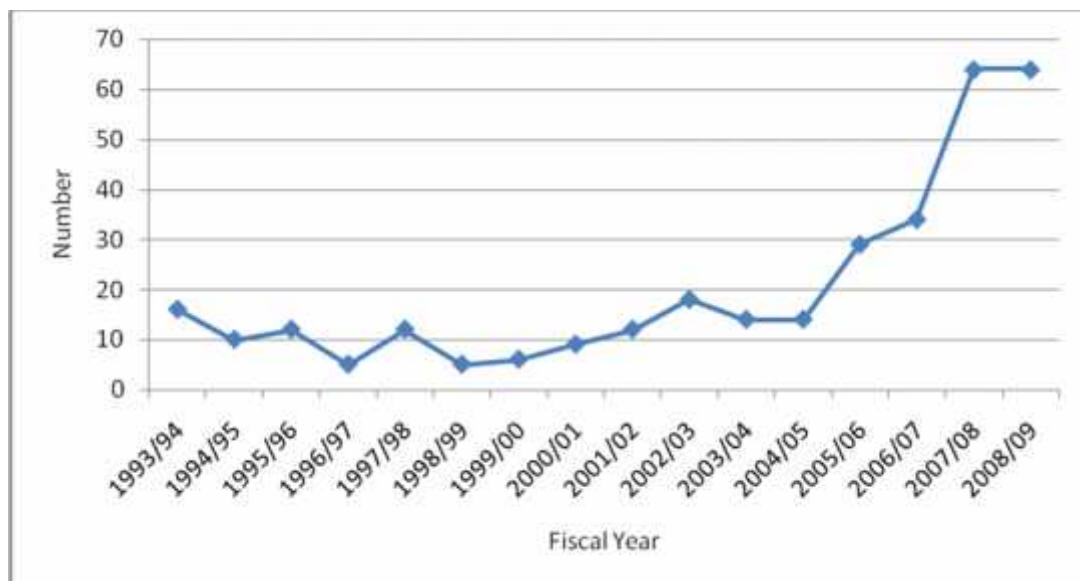


Table 4.1 shows the amount of issue approval, number of issue approval and their percentage of growth from fiscal year 1993/94 to 2008/09. At the beginning fiscal year 1993/94, amount of issue approval, number of issue approval was 244.4 million and 16 respectively. From Table 4.1, the trend of growth of amount of issue approval and number of issue approval seems fluctuating. The lowest and highest amount of issue approval were 174 million and 16828.51 million in the fiscal year 1994/95 and 2008/09 respectively. The annual public issue amount in the fiscal year 2008/09 is about forty times more than that of the fiscal year 1993/94. Similarly, the growth rate of amount of issue approval was highest in the fiscal year 2007/08 i.e. 364.74 percent and lowest growth rate of amount of issue approval was occurred in the fiscal year i.e. declined by 61.40 percent. After the fiscal year 2003/04, the trend of growth rate of amount of issue approval was declining and rose after 2007/08.

**Figure 4.2**  
**Trends of No. of Issue Approval**



From the figure 4.2, it is seen that the lowest number of issue approval was 5 in the fiscal year 1996/97. In the fiscal year 1994/95, 1995/96, 1996/97 and 1997/98, the number of issue approval were 10, 12, 5 and 12 respectively. After onwards, there was increasing trend of number of issue approval from 5 to 18 from fiscal year 1998/99 to 2002/03 which decreased and remained 14 in

fiscal year 2003/04 and 2004/05 and increased to 64 and remained in 2007/08 and 2008/09. The highest number of issue approval was 64 in the fiscal year 2007/08 and 2008/09. Again, the growth rate of number of issue approval was highest in the fiscal year 1997/98 i.e. increased by 140 percent and lowest was in the fiscal year 1996/97 and 1998/99 i.e. declined by 58.33 percent. There was no growth in the fiscal year 2004/05 and 2008/09.

#### **4.1.2 Analysis of Number of Listed Companies**

Number of listed companies is an indicator of size of stock market. The size of stock market increases with the increase in number of listed companies and vice versa. Generally large stock market size indicates a developed stock market. Since listed companies, in Nepalese context are only allowed to issue financial securities and transact their shares in NEPSE. Listing of company is compulsory to make securities trading eligible according to the section 8 of securities exchange Act,1983.

**Table 4.2**  
**Number of Listed Companies**  
**(From fiscal Year 1993/94 to 2008/09)**

| <b>Fiscal Year</b> | <b>Number of Listed Companies</b> | <b>Percentage of Growth</b> |
|--------------------|-----------------------------------|-----------------------------|
| 1993/94            | 66                                | -                           |
| 1994/95            | 79                                | 19.70 %                     |
| 1995/96            | 89                                | 12.66                       |
| 1996/97            | 95                                | 6.74                        |
| 1997/98            | 101                               | 6.32                        |
| 1998/99            | 107                               | 5.94                        |
| 1999/00            | 110                               | 2.80                        |
| 2000/01            | 115                               | 4.55                        |
| 2001/02            | 96                                | -16.52                      |
| 2002/03            | 108                               | 12.50                       |
| 2003/04            | 114                               | 5.56                        |
| 2004/05            | 125                               | 9.65                        |
| 2005/06            | 135                               | 8                           |
| 2006/07            | 135                               | 0                           |
| 2007/08            | 150                               | 11.11                       |
| 2008/09            | 159                               | 6                           |

*Source: Annual Report, SEBON, 2008/09*

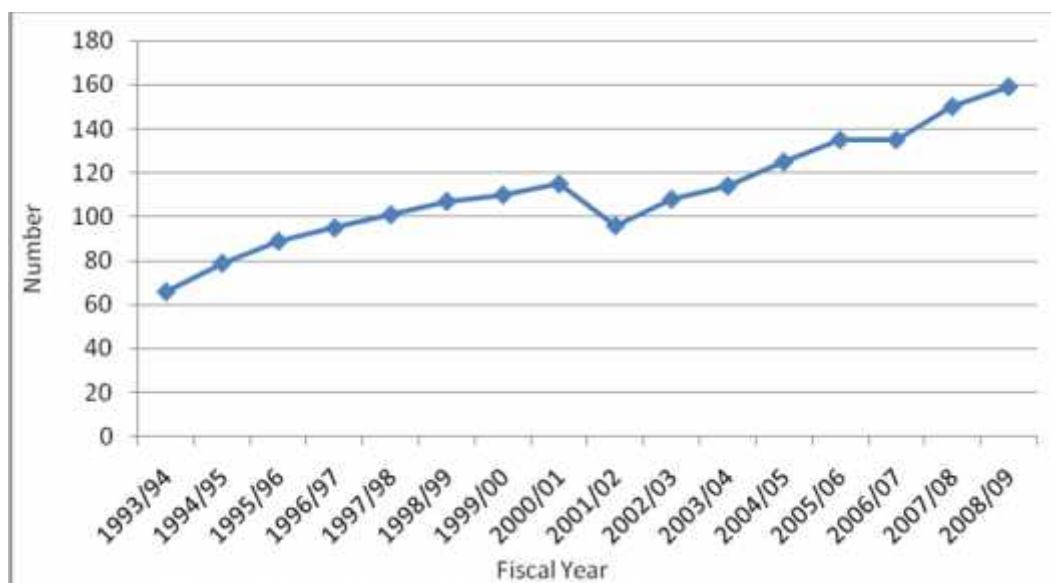
**Figure 4.3****Increase or Decrease in Number of Listed Companies**

Table 4.2 shows the number of listed companies and percentage of growth of number of listed companies from fiscal year 1993/94 to 2008/09. The number of listed companies was 66 in the base year 1993/94. There was increasing trend of listed companies from 66 to 115 from fiscal year 1993/94 to 2000/01 which was decreased to 96 in the fiscal year 2001/02. After that, it increased to 108, 114, 125, 135, 135, 150 and 159 in the fiscal year 2002/03, 2003/04, 2004/05, 2005/06, 2006/07, 2007/08, 2008/09 respectively. However, the number of listed companies is increasing more or less over the period.

From the above Figure, the growth rate of listed companies is all positive over the years except fiscal year 2001/02. The growth rate of number of listed companies was negative i.e. -16.52 percent in the fiscal year 2001/02 because NEPSE deleted some companies from its list because of non – disclosure of fiscal year 1994/95 i.e., 19.70 percent necessary information correctly and timely. The growth rate was highest in fiscal year 1994/95 i.e. 19.70 percent.

#### 4.1.3 Analysis of Paid –up Value

The situation of paid –up value in Nepalese stock market in various years is presented below:

**Table 4.3**  
**Paid –up Value**  
**(From Fiscal year 1993/94 to 2005/06)**

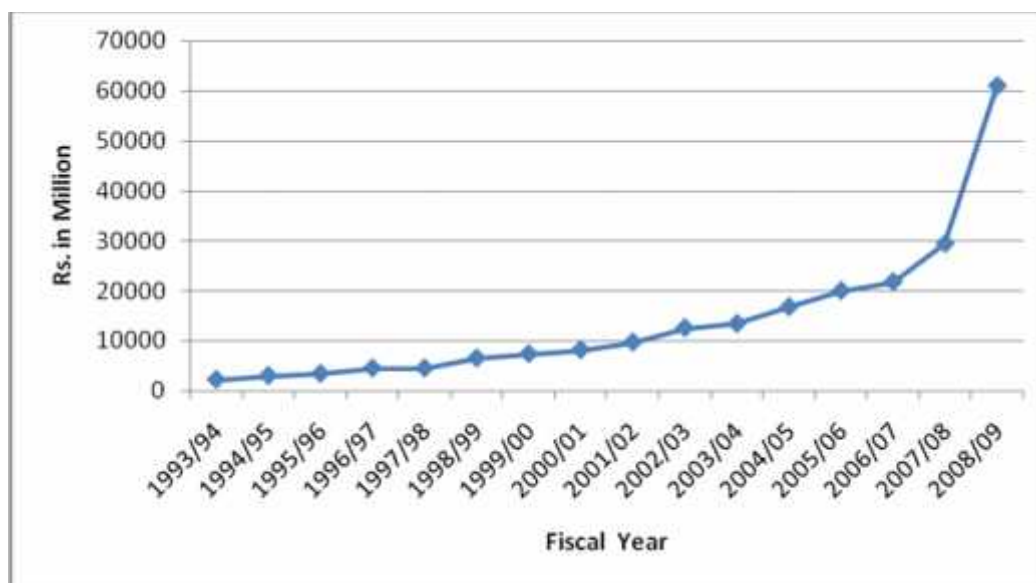
| <b>Fiscal Year</b> | <b>Paid – up Value (Rs in million)</b> | <b>Percentage of Growth</b> |
|--------------------|--|-----------------------------|
| 1993/94            | 2182.2                                 | -                           |
| 1994/95            | 2961.8                                 | 35.73 %                     |
| 1995/96            | 3358.5                                 | 13.39                       |
| 1996/97            | 4476.5                                 | 33.29                       |
| 1997/98            | 4459.9                                 | -0.37                       |
| 1998/99            | 6487.4                                 | 45.29                       |
| 1999/00            | 7347.4                                 | 13.26                       |
| 2000/01            | 8165.2                                 | 11.13                       |
| 2001/02            | 9685.0                                 | 18.61                       |
| 2002/03            | 12560.1                                | 29.69                       |
| 2003/04            | 13404.9                                | 6.73                        |
| 2004/05            | 16771.9                                | 25.12                       |
| 2005/06            | 20008.6                                | 19.30                       |
| 2006/07            | 21798.8                                | 8.95                        |
| 2007/08            | 29465                                  | 35.17                       |
| 2008/09            | 61140.0                                | 107.50                      |

*Source: Annual Report, SEBON, 2008/09*

Table 4.3 and figure 4.4 shows the paid up value and percentage of growth of paid up value from fiscal year 1993/94 to 2008/09. There is increasing trend of paid up value over the period except in fiscal year 1997/98. The paid up value was decreasing from Rs 4476.5 million to Rs 4459.8 million from fiscal year 1996/97 to 1997/98. The highest paid up value was Rs 61140 million in the fiscal year 2008/09 whereas lowest was Rs 2182.2 million in 1993/94.

From the figure, it is seen that the growth rate in fiscal year 1994/95 was 35.73 percent. There was a positive growth rate of paid up value over the period except in the fiscal year 1997/98. The highest growth rate was 107.5 percent in the fiscal year 2008/09 whereas the lowest was negative 0.37 percent in the fiscal year 1997/98.

**Figure 4.4**  
**Increase or Decrease in Paid-up Value**



#### 4.1.4 Analysis of Annual Turnover

**Table 4.4**  
**Annual Turnover**  
**(From Fiscal year 1993/94 to 2008/09)**

| <b>Fiscal Year</b> | <b>Annual Turnover (Rs in million)</b> | <b>Percentage of Growth</b> |
|--------------------|--|-----------------------------|
| 1993/94            | 441.6                                  | —                           |
| 1994/95            | 1054.3                                 | 138.75 %                    |
| 1995/96            | 215.6                                  | -79.55                      |
| 1996/97            | 416.2                                  | 93.04                       |
| 1997/98            | 202.6                                  | -51.32                      |
| 1998/99            | 1500                                   | 640.38                      |
| 1999/00            | 1157                                   | -22.87                      |
| 2000/01            | 2344.2                                 | 102.61                      |
| 2001/02            | 1054.6                                 | -34.28                      |
| 2002/03            | 575.8                                  | -62.62                      |
| 2003/04            | 2144.3                                 | 272.40                      |
| 2004/05            | 4507.7                                 | 110.22                      |
| 2005/06            | 3451.40                                | -23.43                      |
| 2006/07            | 8360.1                                 | 142.22                      |
| 2007/08            | 22820.8                                | 172.98                      |
| 2008/09            | 21681.14                               | -4.99                       |

*Source: Annual Report, SEBON, 2008/09*

**Figure 4.5**  
**Annual Turnover in NEPSE**

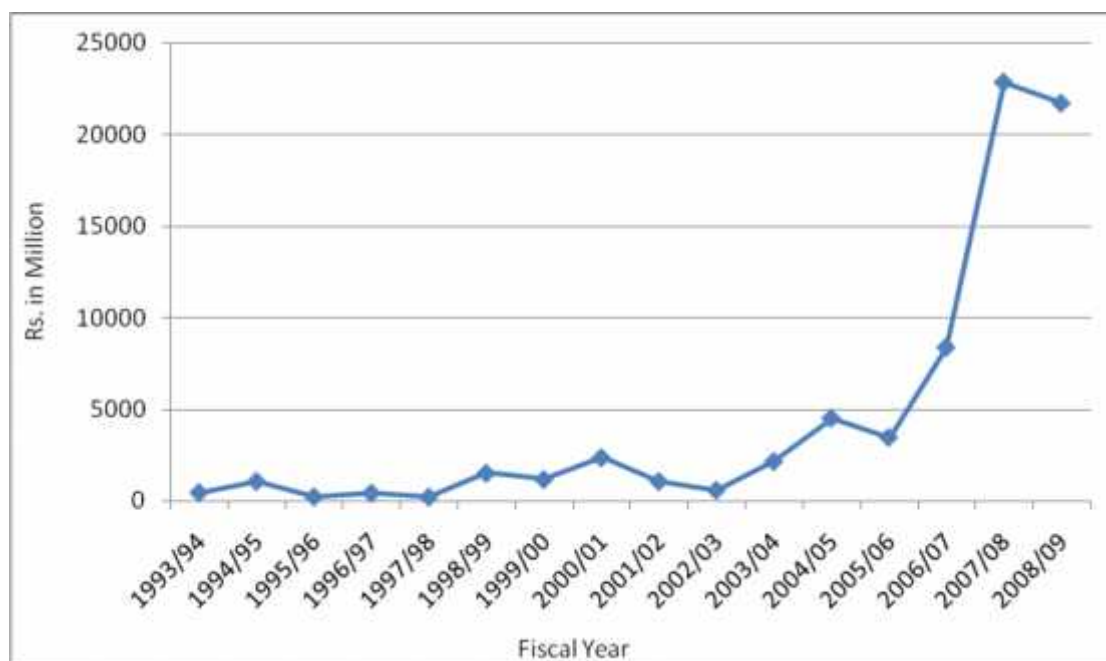


Table 4.4 and Figure 4.5 show the annual turnover in value and percentage of annual turnover from fiscal year 1993/94 to 2008/09. The highest turnover was Rs 22820.8 million in fiscal year 2007/08 where as the lowest turnover was Rs 202.6 million in the fiscal year 1997/98. At the base year 1993/94, Annual turnover was Rs 441.6 million. The trend of amount of annual turnover was fluctuating over the periods.

From the above Figure, it is seen that the trend of growth rate of annual turnover was fluctuating. In the fiscal year 1994/95, the growth rate was 138.75 percent. The highest growth rate was 640.38 percent in the fiscal year 1998/99 and lowest was negative 79.55 percent in the fiscal year 1995/96. In the fiscal year 2008/09, the amount of annual turnover was decreased to 21681.14 million and the growth rate was negative 4.99 percent

#### 4.1.5 Analysis of Market Capitalization in NEPSE

**Table 4.5**  
**Market Capitalization**  
**(From Fiscal year 1993/94 to 2008/09)**

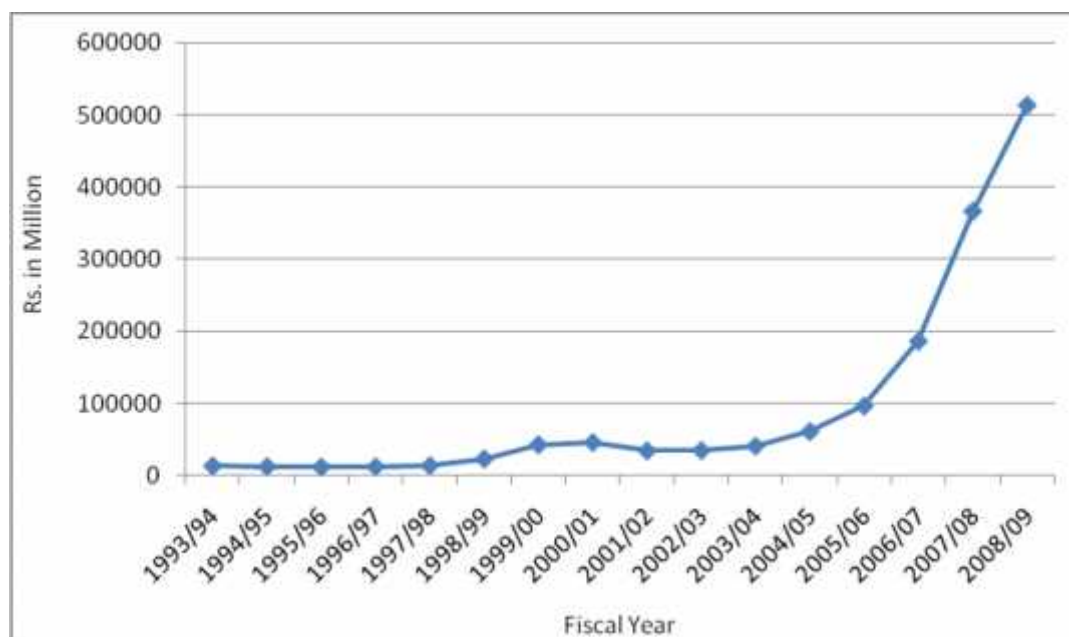
| <b>Fiscal Year</b> | <b>Market Capitalization<br/>(Rs in million)</b> | <b>Percentage of Growth</b> |
|--------------------|--|-----------------------------|
| 1993/94            | 13872  | –                           |
| 1994/95            | 12963  | -6.55 %                     |
| 1995/96            | 12295  | -5.15                       |
| 1996/97            | 12698  | 3.28                        |
| 1997/98            | 14289  | 12.53                       |
| 1998/99            | 23508  | 64.52                       |
| 1999/00            | 43123  | 83.44                       |
| 2000/01            | 46349.40   | 7.48                        |
| 2001/02            | 34703.9  | -25.13                      |
| 2002/03            | 35240.4  | 1.55                        |
| 2003/04            | 41424.3  | 17.55                       |
| 2004/05            | 61365.9  | 48.14                       |
| 2005/06            | 96813.7  | 57.76                       |
| 2006/07            | 186301.3   | 92.43                       |
| 2007/08            | 366247.5   | 96.59                       |
| 2008/09            | 512939.07  | 40.05                       |

*Source: Annual Report, SEBON, 2008/09*

Table 4.5 and Figure 4.6 show the market capitalization of listed securities from fiscal year 1993/94 to 2008/09. The highest market capitalization was Rs 512939.07 million in fiscal year 2008/09 whereas lowest was Rs 12295 million in 1995/96. The market capitalization was decreased from Rs 13872 million to Rs 12295 million from fiscal year 1993/94 to 1995/96 and continuously increased to Rs 46349.4 million in 2000/01. In the fiscal year 2001/02, it decreased to Rs 34703.9 million. Thereafter, there was increasing trend in market capitalization till the fiscal year 2008/09.



**Figure 4.6**  
**Market Capitalization in NEPSE**



From the above Figure, the highest growth rate of market capitalization was 96 percent in the fiscal year 2007/08 and lowest was in 2001/02 i.e. -25.13 percent. It seems that there was all positive growth except in fiscal year 1994/95, 1995/96 and 2001/02 respectively.

#### **4.1.6 Analysis of NEPSE Index**

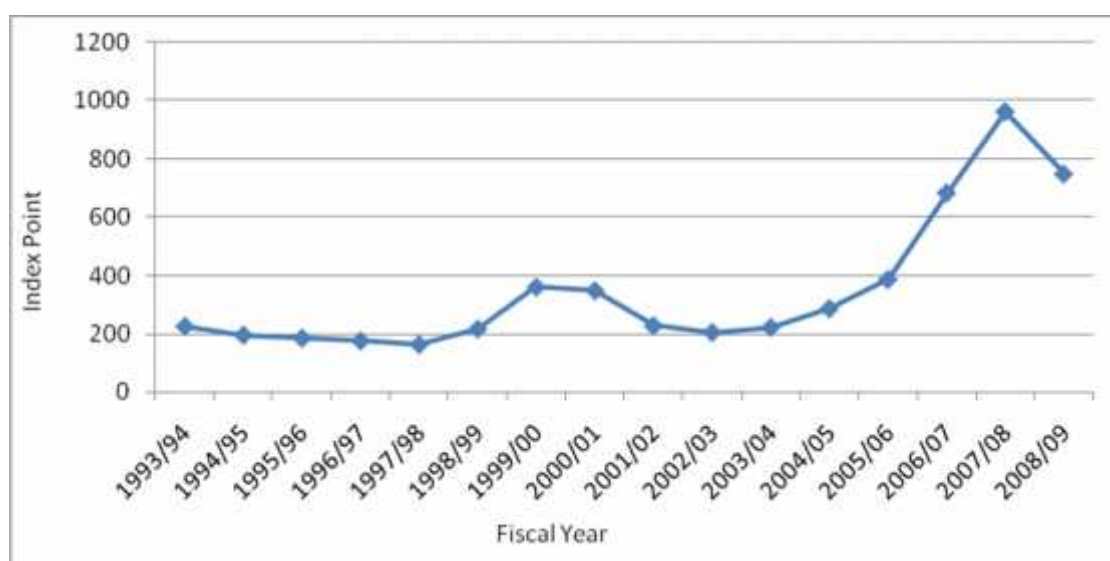
NEPSE Index is the market worth value of all listed companies which is the economic indicator that leads to the investor about the stock market trend. So the higher NEPSE Index indicates the higher return in the stock market and lower NEPSE Index is vice versa. Stock Exchange creates the investment opportunities in the primary as well as secondary market for the investors. In the secondary market, before investing the investor have to inform that the NEPSE Index has its trend and fluctuation of market price of individual stock as well as in aggregate.

**Table 4.6**  
**NEPSE Index**  
**(From fiscal Year 1993/94 to 2008/09)**

| <b>Fiscal Year</b> | <b>Nepse Index Points</b> | <b>Percentage of Growth</b> |
|--------------------|---------------------------|-----------------------------|
| 1993/94            | 226.03                    | –                           |
| 1994/95            | 195.48                    | -13.5 %                     |
| 1995/96            | 185.61                    | -5.02                       |
| 1996/97            | 176.31                    | -5.01                       |
| 1997/98            | 163.35                    | -7.35                       |
| 1998/99            | 216.92                    | 32.80                       |
| 1999/00            | 360.70                    | 66.28                       |
| 2000/01            | 348.43                    | -3.40                       |
| 2001/02            | 227.54                    | -34.69                      |
| 2002/03            | 204.86                    | -9.97                       |
| 2003/04            | 222.04                    | 8.39                        |
| 2004/05            | 286.67                    | 29.11                       |
| 2005/06            | 386.83                    | 34.94                       |
| 2006/07            | 683.95                    | 76.80                       |
| 2007/08            | 963.36                    | 40.85                       |
| 2008/09            | 749.10                    | -22.24                      |

*Source: Annual Report, SEBON, 2008/09*

**Figure 4.7**  
**NEPSE Index**



By analyzing the Table 4.6 and Figure 4.7, it is seen that NEPSE Index in base year i.e. 1993/94 was 226.03. Then after it was declined to 195.48 in 1994/95. The declining trend was continuing to 1997/98. In the fiscal year 1998/99, the NEPSE Index was in increasing trend. It was grown by 32.80 percent and reached to 216.92 whereas the NEPSE Index was only 163.35 in Fiscal year 1997/98. NEPSE Index was 360.70 in the fiscal year 1999/00. Due to the political instability, manipulation in price and most of the listed companies except banking sector not making transaction in capital market, NEPSE Index again had gone downward trend. In the fiscal year 2002, NEPSE Index was 227.54 which were dropped by 34.70 percent from 2001. The NEPSE Index was highest in fiscal year 2007/08 i.e 963.36 and the highest growth rate of NEPSE Index was 76.80 percent in fiscal year 2006/07.

#### 4.1.7 NEPSE Index versus Gross Domestic Product

**Table 4.7**  
**NEPSE Index versus GDP**  
**(From fiscal Year 1993/94 to 2008/09)**

| <b>Fiscal Year</b> | <b>NEPSE Index</b> | <b>Percentage of Growth in NEPSE Index</b> | <b>Gross Domestic Product (Rs in million)</b> | <b>Percentage of Growth in GDP</b> |
|--------------------|--------------------|--|---|------------------------------------|
| 1993/94            | 226.03             | —  | 191596  | -                                  |
| 1994/95            | 195.48             | -13.5 %                                    | 209976  | 9.59%                              |
| 1995/96            | 185.61             | -5.02                                      | 339388  | 14.01                              |
| 1996/97            | 176.31             | -5.01                                      | 269570  | 12.61                              |
| 1997/98            | 163.35             | -7.35                                      | 289798  | 7.50                               |
| 1998/99            | 216.92             | 32.80                                      | 330018  | 13.88                              |
| 1999/00            | 360.70             | 66.28                                      | 366251  | 10.98                              |
| 2000/01            | 348.43             | -3.40                                      | 394052  | 7.59                               |
| 2001/02            | 227.54             | -34.69                                     | 406138  | 3.07                               |
| 2002/03            | 204.86             | -9.97                                      | 437546  | 7.73                               |
| 2003/04            | 222.04             | 8.39                                       | 474919  | 8.54                               |
| 2004/05            | 286.67             | 29.11                                      | 508651  | 7.10                               |
| 2005/06            | 386.83             | 34.94                                      | 557869  | 9.68                               |
| 2006/07            | 683.95             | 76.80                                      | 728178.0                                      | 30.53                              |
| 2007/08            | 963.36             | 40.85                                      | 818402.0                                      | 12.39                              |

|         |        |        |          |       |
|---------|--------|--------|----------|-------|
| 2008/09 | 749.10 | -22.24 | 960012.0 | 17.30 |
|---------|--------|--------|----------|-------|

*Source: Annual Report, SEBON, 2008/09*

*Economic Survey, Ministry of Finance, 2008/09*

Table 4.7 shows the percentage of growth of NEPSE Index and percentage of growth of GDP from fiscal year 1993/94 to 2008/09. In comparison with growth rate of NEPSE Index and growth rate of GDP, growth rate of GDP was always better than growth rate of NEPSE except in fiscal year 1998/99, 1999/00, 2004/05, 2005/06, 2006/07 and 2007/08. In that year growth rate of NEPSE were 32.80, 66.28, 29.11, 34.94, 76.80 and 40.85 percent whereas the growth rate of GDP were 13.88, 10.98, 7.10, 9.68, 30.53 and 12.39 percent respectively. If we take only the growth rate of GDP in that year, the rates were more or less satisfactory but in comparison with NEPSE Index's growth rate it was lower than that.

Most of the years, the growth of NEPSE Index were in downward trend i.e. negative. This is because of the problem faced by Nepalese Stock market. All the listed companies cannot do well except some commercial banks. But on the other side of GDP, it was in increasing trend. Due to the problems of political instability, weak law and other situations, the growth rate of GDP was, however, more or less satisfactory. The highest growth rate of GDP was in the fiscal year 2006/07 i.e. 30.53 and lowest growth rate was in the fiscal year 2001/02 i.e. only 3.07 percent growth from the last fiscal year's 7.59 percent. Similarly in NEPSE Index, the highest growth rate was in the fiscal year 2006/07 i.e. 76.80 percent and lowest growth rate in NEPSE was in the year 2001/02 i.e. negative 34.69 percent. Although, there is no direct relationship between NEPSE Index and GDP, the increase or decrease in national GDP affects the NEPSE Index and vice versa.

#### **4.1.8 Market Capitalization versus Gross Domestic Product**

Another important measure of the stock market size is the market capitalization ratio which is the aggregate market value of the listed shares divided by Gross

Domestic Product. This ratio indicates the relative importance of stock market to the national economy and assumes that stock market size is positively correlated with the ability to mobilize capital and diversify risk.

**Table 4.8**  
**Market Capitalization versus GDP**  
**(From Fiscal year 1993/94 to 2008/09)**

| <b>Fiscal Year</b> | <b>Market Capitalization (Rs in million)</b> | <b>Gross Domestic Product (Rs in million)</b> | <b>Percentage of Market capitalization on Nominal GDP</b> |
|--------------------|--|---|---|
| 1993/94            | 13872  | 191596  | 7.24%   |
| 1994/95            | 12963  | 209976  | 6.17  |
| 1995/96            | 12295  | 339388  | 5.14  |
| 1996/97            | 12698  | 269570  | 4.71  |
| 1997/98            | 14289  | 289798  | 4.93  |
| 1998/99            | 23508  | 330018  | 7.12  |
| 1999/00            | 43123  | 366251  | 11.77   |
| 2000/01            | 46349.40                                     | 394052  | 11.76   |
| 2001/02            | 34703.9                                      | 406138  | 8.55  |
| 2002/03            | 35240.4                                      | 437546  | 8.05  |
| 2003/04            | 41424.3                                      | 474919  | 8.72  |
| 2004/05            | 61365.9                                      | 508651  | 12.06   |
| 2005/06            | 96813.7                                      | 557869  | 17.35   |
| 2006/07            | 186301.3                                     | 728178.0                                      | 25.58   |
| 2007/08            | 366247.5                                     | 818402.0                                      | 44.75   |
| 2008/09            | 512939.07                                    | 960012.0                                      | 53.43   |

*Source: Annual Report, SEBON, 2008/09*

*Economic Survey, Ministry of Finance, 2008/09*

From the table 4.8, market capitalization ratio on nominal GDP was 7.24 percentages in base year 1993/94 but it started to decrease gradually and dropped to 4.71 percent in the fiscal year 1996/97. The figure of 4.71 percent was the lowest market capitalization ratio during the sixteen years observation period. And, then the market capitalization ratio increased by 0.22, 2.41 and 7.06 percent on the ratio of fiscal year 1996/97. As a result the ratio appeared 11.77 percent in fiscal year 1999/00. The ratio remained 11.76 percent in fiscal year

2000/01 but it again drastically decreased to 8.55 percent in fiscal year 2001/02 and 8.05 percent in fiscal year 2002/03. Thereafter it slightly increased year to year and reached to 17.35 in the fiscal year 2005/06 and then after it increased drastically continually. The highest market capitalization ratio over the last sixteen years period is 53.43 in fiscal year 2008/09.

Although, the highest market capitalization ratio of 53.43 percent in fiscal year 2008/09 is better ratio than other fiscal years. It is very poor than other developing and developed countries because it lies between 20 percent to 40 percent in many developing countries and it is greater than 100 percent in developed countries. Thus, it can be concluded that the growth of stock market is low relative to its economy.

#### **4.2 Presentation and Analysis of Primary Data**

The analysis of primary data collected through questionnaire is presented in this section. The questionnaires were distributed to investors and finance students in order to identify their opinions with respect to Growth, Problem and Prospects of stock market in Nepal. Respondents from financial and non financial experts, staffs of SEBON, stock brokers, investors and finance students participated in this survey.

50 questionnaires were distributed among them. Out of them, 10 questionnaires were distributed to financial experts and only 8 questionnaires were received. Similarly 10 to SEBON's staff, 10 to rational investor, 5 to stock broker, 5 to finance teacher and rest questionnaires were distributed to finance students. However, 10 from staff of SEBON, 6 from investors, 4 from stock broker, 4 from finance teacher and 8 questionnaires from finance students were received. The responses of each choice in the question where the choices are to be ranked are weighted by the value of the rank assigned by the respondents. And weighted arithmetic means were calculated to find out the overall rank for each choice for the respondents.

#### 4.2.1 Analysis of Growth of Nepalese Stock Market

Overall growth of Nepalese stock market has been analyzed on the basis of growth of number of listed company, amount of market capitalization, amount of IPO, number of issue manager and brokers and low level of industrialization and small volume of security traded etc. Growth measurement –base statements and their mean score has been presented in Table 4.9.

**Table 4.9**

#### **Result of mean score of survey of growth of Nepalese Stock Market**

| S.N | Statement  | 5  | 4  | 3  | 2  | 1 | Mean Score |
|-----|--|----|----|----|----|---|------------|
| 1   | The growth of number of listed company is satisfactory.  | 2  | 6  | 3  | 21 | 8 | 2.325      |
| 2   | The growth of market capitalization is satisfactory.   | 17 | 10 | 6  | 5  |   | 4.075      |
| 3   | The growth of amount of IPO is satisfactory.   | 3  | 11 | 17 | 9  |   | 3.2        |
| 4   | Increase in number of institutional investors in stock market is satisfactory.                           | 26 | 13 |    | 2  |   | 4.6        |
| 5   | Number of issue manager and brokers are not sufficient.  | 16 | 20 | 4  |    |   | 4.3        |
| 6   | Low level of industrialization and small volume of securities traded hinders the growth of stock market. | 6  | 6  | 10 | 8  |   | 3.25       |

As far as the growth of number of listed company is concerned, mean score is 2.325. Mean score is nearest to 2 which means respondents think that growth rate of number of listed company is not satisfactory. On the other hand, Respondents are asked to rank the growth of market capitalization. The mean score is 4.075 which means that respondents are clearly say that the growth rate of market capitalization is satisfactory. Again, regarding the growth amount of IPO, mean score is 3.2 which is nearest to 3. It indicates that most of the respondents cannot clearly say the growth amount of IPO is satisfactory or not.

On the other hand, respondents are asked to rank the increase in number of institutional investors in stock market, mean score of it is 4.6, It means that they are strongly agree with that the increase in institutional investors in stock market is satisfactory. Similarly the respondents are agreeing with the statement that number of issue manager and brokers are not sufficient. So mean score of this statement is 4.3. But, most of the respondents don't want to say low level of industrialization and small volume of securities traded hinders the growth of stock market. So they ranked it at the point don't know. So the mean scores become 3.25.

#### 4.2.2 Analysis of Problems of Nepalese Stock Market

The problems of Nepalese Stock market has been analyzed on the basis of legal rules and regulations, availability of information, influenced by small number of large investors, special provisions to attract institutional investors, number of issue managers and brokers, characteristics of rumor based market, insufficient knowledge of investors about the stock market and lack of professionalism in brokers. Problem measurement-base statement and their mean score are presented in table 4.10.

**Table 4.10**  
**Result of mean score of survey of Problems of Nepalese Stock Market**

| SN. | Statement   | 5  | 4  | 3  | 2 | 1 | Mean Score |
|-----|---|----|----|----|---|---|------------|
| 1   | Legal rules and regulations are not sufficient.                                   | 24 | 10 | 2  |   | 2 | 4.6        |
| 2   | Information is not easily available to investors.                                 | 8  | 24 | 8  |   |   | 4          |
| 3   | Stock market is greatly influenced by small number of large investors.            | 17 | 17 |    | 2 | 4 | 4.0250     |
| 4   | There is no special provision to attract institutional investors in stock market. | 17 | 16 | 7  |   |   | 4.0250     |
| 5   | Number of issue managers and brokers are not sufficient.                          | 16 | 14 | 6  | 4 |   | 4.05       |
| 6   | The need of new stock exchange is now realized by investors.                      | 4  | 20 | 14 |   |   | 3.35       |
| 7   | Nepalese stock market is the characteristics of rumor based market.               | 7  | 26 | 5  | 2 |   | 4.10       |



|   |  |    |    |   |  |   |       |
|---|--|----|----|---|--|---|-------|
| 8 | There is insufficient knowledge of investor about the stock market.              | 10 | 23 | 7 |  |   | 4.075 |
| 9 | Lack of professionalism in brokers has hindered the development of stock market. | 16 | 23 |   |  | 1 | 4.35  |

As regarding with the legal rules and regulations are not sufficient, mean score is 4.6 which is nearest to 5. It means that most of respondents are strongly agree with the statement. Similarly, respondents are asked to rank the statement i.e. information is not easily available to investors. The mean score of the statement is exactly 4. Regarding the stock market is greatly influenced by small number of large investors; the mean score is 4.025 which are nearest to 4. It means that respondents are agreed with the statement. Another point, there is no special provision to attract institutional investors in stock market, respondents are also agree with this statement. So its mean score is also 4.025. As far as concerned with the number of issue managers and brokers are not sufficient, mean score is 4.05. It indicates that they feel that it is the important problem of Nepalese stock market. On the other hand, the respondents are asked to rank the statement that the need of new stock exchange is now realized by investors, the mean score is 3.05. It means that they can not clearly say that whether it is agree or disagree. Regarding the Nepalese stock market is the characteristics of rumor based market, the majority of respondents are agree with the statement and its mean score becomes exactly 4. Similarly, Most of the respondents are agree with the statement no. 8 and 9. Its mean score are 4.075 and 4.35 which indicates that insufficient knowledge of investors and lack of professionalism in brokers are the vital problem of Nepalese stock market.

#### **4.2.3 Analysis of Prospects of Nepalese Stock Market**

Regarding the prospects of Nepalese stock market, respondents are asked to rank the different measurement base statements. These are based on the number of listed company and turnover of listed companies, return from the stock market, growth amount of IPO, general provision, investor awareness' program launched by SEBON, liquidity and marketability, trend of large companies

listed in NEPSE and interest of educated and business people, Government policy towards the stock market and on-site and off-site inspection conducted by SEBON. These are analyzed with the help of mean score. The Prospects measurement –base statement and their mean score is presented in table 4.11.

**Table 4.11**

**Result of mean score of survey of Prospects of Nepalese Stock Market**

| S.N | Statement  | 5  | 4  | 3  | 2  | 1  | Mean Score |
|-----|--|----|----|----|----|----|------------|
| 1   | The number of listed companies and turnover of listed companies is increasing yearly.  | 17 | 4  | 6  | 4  |    | 4.075      |
| 2   | Stock market provides satisfactory return.   | 12 | 20 | 4  | 4  |    | 4          |
| 3   | The growth of amount of IPO is increasing.   | 9  | 24 | 6  | 1  |    | 4.025      |
| 4   | Legal provision has become easier and improved in comparisons to past years.   | 1  | 10 | 6  | 19 | 4  | 2.625      |
| 5   | General provisions are becoming aware about stock market.  | 3  | 10 | 20 | 7  |    | 3.225      |
| 6   | An investor awareness program launched by SEBON is successful.   | 4  | 9  | 22 | 3  | 2  | 3.25       |
| 7.  | Liquidity and marketability is the main factor to develop the stock market.  | 13 | 18 | 4  | 5  |    | 4          |
| 8.  | Trend of large companies listed in NEPSE and increasing interest of educated and business people are greater prospect for Nepalese stock market. | 14 | 18 | 6  | 2  |    | 4.10       |
| 9.  | Government has taken the policy of dynamic transparent, credible and investor friendly stock market.   | 2  | 5  | 10 | 13 | 10 | 2.4        |
| 10. | One-site inspection and off-site inspection conducted by SEBON is good news for investors.   | 2  | 12 | 16 | 10 |    | 3.15       |

As evident from table 4.11, the mean score of statement no.1 is 4.075 which indicate that respondents are agreed with the number of listed companies and turnover of number of listed company. Similarly, incase of stock market provides satisfactory return; the mean score is 4 which indicates the respondents are agreed with the statement. When respondents are asked to rank the growth amount of IPO, The mean score of it is 4.025, It means that they agree with the growth amount of IPO is increasing. These are the main

prospects of stock market. On the other hand some statements based on legal provision, general provision and investor awareness program launched by SEBON, respondents are not clearly say that they are agree or disagree. So, they rank it as don't know and their mean score are 2.625, 3.225 and 3.25. It means that Nepalese investors are not aware about the rules and regulation and program launched by SEBON. As far as the liquidity and marketability is the main factor to develop the stock market, the mean score is 4 which means respondents are agreed with it. Based on that point, one of the reasons to invest in stock is liquidity and marketability. Similarly, regarding the trend of large company listed in NEPSE and increasing interest of educated and business people .The mean score is 4.0 which is nearest to 4. It means that most of the respondents are agree with this statement. But incase of the policy taken by government, mean score is 2.4 which is nearest to 2. Respondents ranked it as disagree. It indicates that Government has not taken the dynamic and investor friendly policy. Another statement regarding the inspection conducted by SEBON is good news for investors, mean score is 3.15. In this case, respondents are not clearly stands on the point agree or disagree, it means that they are not aware about that statement. So it is concluded that the inspection program conducted by SEBON is not successful.

### **4.3 Major Findings of the Study**

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

1. From the analysis of growth of Nepalese stock market, it can be concluded that growth of market capitalization and growth in number of market capitalization and growth in number of institutional investor are satisfactory. However, majority of the respondents are not satisfied with the growth in number of listed companies. On the other hand, respondents are not certain whether growth amount of IPO and growth in volume of security traded is satisfactory or not.

2. The investors are facing several problems and difficulties during their transaction period .The majority of the respondents are agreed with the asked statements. So it was concluded that main problem of stock market are insufficiency of legal rules and regulations, unavailability of information, influenced by small number of large investors , in sufficiency of number of issue managers, rumor based market, insufficient knowledge of investors etc. However, the respondents are not realized the need of new stock exchange.
3. By analyzing the prospects of Nepalese stock market, it can be concluded that increase in number of listed companies and turnover of listed companies, return from the stock market, increase in amount of IPO and increase in trend of larger companies listed are main factor for the prospects of Nepalese Stock Market.
4. However, the majority of respondents cannot say general provisions are becoming easy or not, program launched by SEBON is successful or not etc. Most investors are not satisfied with the policy of dynamic, transparent credible and investor friendly stock market taken by government.
5. The amount of issue approval in base year was 244.4 million which is increased to 16828.51 million in fiscal year 2008/09. The growth rate of amount of issue approval was all positive except in fiscal year 1994/95,1998/99,2002/03 and 2006/07 .So the amount of issue approval is more or less satisfactory.
6. The number of issue approval was increased from 16 to 64 from fiscal year1993/94 to 2008/09. The growth rate of number of issue approval was fluctuating over the periods. So it can be concluded that growth of number of issue approval is not satisfactory.
7. The total number of listed companies reached from 66 to 159 in fiscal year2008/09. The growth rate of listed companies is all positive (even zero in 2006/07) except in the fiscal year 2001/02 because NEPSE deleted some companies from its list because they did not disclose necessary

information timely and correctly. It can say that number of listed companies is satisfactory.

8. The paid-up value of listed securities is highest in 2008/09 with Rs 61140 million and lowest in year 1993/94 with 2182.2 million. The growth rate of paid-up value is all positive except in fiscal year 1997/98.
9. The highest annual turnover in value was 22820.8 million in the fiscal year 2007/08 and lowest annual turnover was Rs 202.6 million in the fiscal year 1997/98. The trend of growth rate of annual turnover was fluctuating. The highest growth rate was 640.38 percent in the fiscal year 1998/99 and lowest was negative 79.55 percent in the fiscal year 1995/96.
10. The market capitalization of listed securities was Rs 13872 million in the base year 1993/94 and Rs 512939.07 million in fiscal year 2008/09. The highest growth rate of market capitalization was 96.59 percent in the fiscal year 2007/08. And lowest was in 2002/03 i.e. negative 25.13 percent. It is found that there was all positive growth except in fiscal year 1994/95, 1995/96 and 2001/02 respectively.
11. NEPSE Index continuously declined after its establishment in 1993 till the fiscal year 1997/98. Then it was in increasing trend till 2001. Due to the weak law and difficult situation, industrial service and trading sector cannot do well. So NEPSE Index also was in decreasing trend again up to the fiscal year 2002/03. After that there was increasing trend of NEPSE Index because of political consensus has built up and index reached up to 683.95 in fiscal year 2008/09.
12. The highest market capitalization ratio of 53.43 percent in fiscal year 2008/09 is better ratio than other fiscal years. Thus, it can be concluded that the growth of stock market is growing relative to its past experience.
13. By analyzing the overall aspect of stock market, it is found that the stock market is suffering from various problems. The growth of Nepalese stock market is satisfactory and the prospect of stock market is equally strong if

the government has taken the transparent credible and investor friendly policy.

## **CHAPTER - V**

### **SUMMARY, CONCLUSION AND RECOMMENDATION**

In the previous chapters, researchers explained the introduction, review of literature research methodology and presentation and analysis of data. This chapter presents the summary, conclusions and recommendations from the analysis of primary and secondary data regarding the growth, problems and prospects of Nepalese stock market.

#### **5.1 Summary**

Stock market in recent years has become an integral part of economic development. It can play a vital role in encouraging and channeling the saving to provide the entrepreneurs for investment in profitable projects in the economy. Examples from the developed countries have proved that the stock market is the cause and economic development is the effect. Stock market serves as a direct link between the suppliers and the users of capital fund. Thus, stock market has both theoretical and practical perspectives. This study mainly aims to examine the situation of stock market in Nepal. The specific objectives of the study are to examine the growth of Nepalese stock market, to identify the problems and challenges of stock market and to analyze the prospects of stock market in Nepal.

This study is based on both secondary and primary data analysis. The required secondary data are collected from the annual report of SEBON and its web site: <http://www.sebo@ntc.np>, the trading report of NEPSE and its web site: <http://www.nepalstock.com>, Nepal Rastra Bank etc. For the further support of this study, survey of questionnaire from various respondents and indirect interview of officers of related authority and investors have been taken.

Both historical and descriptive research design are carry out this study. The growth of Nepalese stock market is examined on the basis of amount of issue

approval, number of issue approval, number of listed companies, annual turnover, market capitalization and paid –up value. Primary data are analyzed on the basis of Likert scale using various measurement-base statements.

During the fiscal year 1993/94, the annual turnover is in fluctuating manner. The number of listed companies is in increasing trend except in the fiscal year 2001/02. The number of issue approval and amount of issue approval are more or less satisfactory. Amount of issue approval was in increasing trend after the fiscal year 2002/03. Similarly, amount of market capitalization and paid-up value are in increasing trend. The growth of NEPSE Index was in fluctuating manner due to the decline in the investor's confidence level on the capital market.

From the analysis of primary data, it is seen that number of issue managers and brokers are not sufficient. The growth of market capitalization is satisfactory. Most of the respondents are agree with following statements, legal rules and regulations are not sufficient. Information is not easily available to investors; Stock market is greatly influenced by small number of large investors. There is no special provision to attract institutional investors in the stock market. Nepalese stock market is the characteristics of rumor based market. There is insufficient knowledge of investor about the stock market which is the major problems of the Nepalese stock market. Stock market has also seen many prospects from the survey. They are: the number of listed companies and turnover of listed companies are increasing yearly, most of the respondents are agreed with stock market provides satisfactory return, the growth amount of IPO is increasing, and stock market provides liquidity and marketability. Similarly trend of large companies listed in NEPSE and increasing interest of educated and business people are the greater prospects for Nepalese stock market.



## 5.2 Conclusion

The development of stock market in Nepal so far cannot be considered satisfactory. This is evident from the facts and figures available in the stock market performance during the last sixteen years. This study concludes that the growth rate of amount of issue approval were more or less satisfactory. The number of issue approval was fluctuating manner over the periods. So, the growth rate of number of issue approval was not satisfactory. Similarly, growth rate of number of listed companies are all positive except in one year. The trend of paid-up value is increasing. But annual turnover value, NEPSE Index and market capitalization are fluctuating. This indicate that the situation of growth of stock market in Nepal. On the other hand, it concludes that the investors are facing several problems and challenges during the transaction period. It is concluded that the major problems of the stock market are insufficiency of legal rules and regulations, unavailability of information, influenced by small number of large investors, insufficient number of brokers and issue managers rumor based market, insufficient knowledge of investors etc. However, from the analysis of the study, the investors are not realized the need of new stock exchange.

From the analysis of prospects of Nepalese Stock Market, it is resulted that increase in number of listed companies, satisfactory return from the stock market, increasing amount of initial public offerings, increasing trend of large companies listed in NEPSE and increasing interest of educated and business people are the major prospects of Nepalese stock market. General provision taken by government, on-site and off-site inspection program launched by SEBON are the minor prospects of Nepalese stock market. However the transparency and openness of transaction, quality professional services, adequate corporate financial disclosures and improved legal regulatory and supervisory are the urgent need of Nepalese Stock Market. The government has to play major role to encourage individual as well as institutional investors' participation and sustaining in stock market any effort for protecting investors

interest or boosting their confidence or developing the stock market is necessary, that should be enabled to operate in an environment that leads to growth and expansion of Nepalese Stock Market.

### **5.3 Recommendation**

Based on the analysis of primary and secondary data, this study has reached to the following recommendations:

1. The Securities Board of Nepal has the responsibility of regulating the entire securities market in Nepal. To make the Board effective, the number of staff should be adequate and properly trained in all aspects of securities market. It should bring new and emerging stock market regulatory regimes to match international standards.
2. The number of listed companies is increasing every year but the increase is not proportionately among the various sectors. Out of the total increase, the numbers of banks and finance companies have dominated. So the government should bring new policy to attract more manufacturing and processing, trading and other companies to come in the public and to list their securities in the stock exchange.
3. The market is totally dominated by corporate securities. So to increase the breadth of the market, more government securities must list in Nepal Stock Exchange.
4. Involve in high cost in public offering is the reasons for corporate bodies not going for public. So, the following steps should be taken to bring down the cost of public issue:
  - ) As the shares are over subscribed, the relevant securities laws and regulations should be amended.
  - ) The minimum number of days allowed for subscription for public should be brought down to three working days from seven working days.
  - ) The procedures for offering public issue should be simplified and rationalized. There should not be overlapping requirements.

5. There is need to provide the opportunity for a large number of investors to participate directly or through mutual saving scheme, which ultimately enhance the breadth and depth of the stock market.
6. The Nepalese stock market should take some initiation to establish the system of regular monitoring and evaluation of stock market.
7. From the researcher view point only, it is known that there is urgency of expansion of NEPSE services to the regional levels rather than just concentrating solely in the valley.
8. There should be efficient coordination and cooperation among Securities Board and Nepal Rastra Bank in order to develop the stock market.
9. Current manual method of securities trading system should be replaced with computer based technology which will enhance the pace of trading activities.
10. Nepalese Stock Market is suffered from rumor based market and inadequate knowledge of investors, unavailability of information, influenced by small number of large investors. So many programs should be launched by concerned authority.
11. This study reveals the weak performance of stock market and slow pace of development. So several efforts should be made to reform the market and improve market performance.

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### Websites:

[www.nepalstock.com](http://www.nepalstock.com)

[www.sebonp.com](http://www.sebonp.com)

**Appendix**  
**Questionnaires on Growth, Problems and Prospects of Nepalese stock Market**

Dear Respondent,

I am an MBS final year student. The MBS program of faculty of management, T.U requires the students to write a thesis for which I am conducting a survey of A STUDY ON NEPALESE STOCK MARKET IN THE LIGHT OF ITS GROWTH, PROBLEMS AND PROSPECTS. I would highly appreciate your kind cooperation regarding the matter.

Thank you  
Suman Dahal

Name (optional):

Position:

Institution:

Address:

Phone no:

**Part A: Growth of Nepalese Stock Market**

*How far do you agree/disagree with the following observations on growth of Nepalese stock market? (Please make a tick- mark at the appropriate number as per following scheme: 5 = strongly agree; 4 = agree; 3 = do not know, 2 = disagree, and 1 = strongly disagree.)*

| S.N. | Statement  | 5 | 4 | 3 | 2 | 1 |
|------|--|---|---|---|---|---|
| 1    | The growth of number of listed company is satisfactory.  |   |   |   |   |   |
| 2    | The growth of market capitalization is satisfactory.   |   |   |   |   |   |
| 3    | The growth of amount of IPO is satisfactory.   |   |   |   |   |   |
| 4    | Increase in institutional investors is necessary condition for the growth of stock market.               |   |   |   |   |   |
| 5    | Number of issue manager and brokers are not sufficient.  |   |   |   |   |   |
| 6    | Low level of industrialization and small volume of securities traded hinders the growth of stock market. |   |   |   |   |   |

**Part B: Problems of Nepalese Stock Market**



*How far do you agree/disagree with the following observations on problems of Nepalese stock market? (Please make a tick- mark at the appropriate number as per following scheme: 5 = strongly agree; 4 = agree; 3 = do not know, 2 = disagree, and 1 = strongly disagree).*

| S No. | Statement   | 5 | 4 | 3 | 2 | 1 |
|-------|---|---|---|---|---|---|
| 1     | Legal rules and regulations are not sufficient.                                   |   |   |   |   |   |
| 2     | Information is not easily available to investors.                                 |   |   |   |   |   |
| 3     | Stock market is greatly influenced by small number of large investors.            |   |   |   |   |   |
| 4     | There is no special provision to attract institutional investors in stock market. |   |   |   |   |   |
| 5     | Number of issue managers and brokers are not sufficient.                          |   |   |   |   |   |
| 6     | The need of new stock exchange is now realized by investors.                      |   |   |   |   |   |
| 7     | Nepalese stock market is the characteristics of rumor based market.               |   |   |   |   |   |
| 8     | There is insufficient knowledge of investor about the stock market.               |   |   |   |   |   |
| 9     | Lack of professionalism in brokers has hindered the development of stock market.  |   |   |   |   |   |

### Part C: Prospects of Nepalese Stock Market

*How far do you agree/disagree with the following observations on prospects of Nepalese stock market? (Please make a tick- mark at the appropriate number as per following scheme: 5 = strongly agree; 4 = agree; 3 = do not know, 2 = disagree, and 1 = strongly disagree.)*

| S.N. | Statement  | 5 | 4 | 3 | 2 | 1 |
|------|--|---|---|---|---|---|
| 1    | The number of listed companies and turnover of listed companies is increasing yearly.  |   |   |   |   |   |
| 2    | Stock market provides satisfactory return.   |   |   |   |   |   |
| 3    | The growth of amount of IPO is increasing.   |   |   |   |   |   |
| 4    | Legal provision has become easier and improved in comparisons to past years.   |   |   |   |   |   |
| 5    | General provisions are becoming aware about stock market.  |   |   |   |   |   |
| 6    | An investor awareness program launched by SEBON is successful.   |   |   |   |   |   |
| 7.   | Liquidity and marketability is the main factor to develop the stock market.  |   |   |   |   |   |
| 8.   | Trend of large companies listed in NEPSE and increasing interest of educated and business people are greater prospect for Nepalese stock market. |   |   |   |   |   |
| 9.   | Government has taken the policy of dynamic transparent, credible and investor friendly stock market.   |   |   |   |   |   |
| 10.  | One-site inspection and off-site inspection conducted by SEBON is good news for investors.   |   |   |   |   |   |