A Study on Cointegration between Indian and Chinese Stock Markets

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Abstract

The objective of this study is to analyze the connections that exist amongst the Indian & the Chinese Stock Markets. To find the presence & the extent of co movement, Cointegration analysis of Indian and the Chinese stock markets has been made over 15 years time period using Johansen test of Cointegration. The results of the study reveal that there exists long causality amongst the two stock markets. As regards the short run causality, Chinese stock market affect the Indian stock market in short run but this is not the case with the Indian stock market. Thus, there is long run bidirectional causality between the two markets but unidirectional short run causality. In case of disequilibrium, Chinese markets adjust faster towards equilibrium. For an investor, the study has provided useful insight for investment. The result of the study reveal the fact that an investor will not likely get any benefit of diversifying portfolio between the two stock markets since the two markets show evidence of moving in the same direction in long run.

I. Introduction

WITH GLOBALIZATION AND Liberalization of restrictions on international flow of capital and trade, Indian market is expected to be more integrated with other stock markets of the world. Liberalization and Globalization and the development in information technology has paved the way for more trade and inflow of foreign capital into the country. The world has become a global village. Economic linkages have intensified. Any happening in one part of the world influences the part either directly or indirectly. This paper aims to contribute to our understanding of the globalization and integration of two developing Asian stocks markets namely India and China.

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The result of Wald test shows that all the coefficients of the Nifty index taken together are insignificant which means the Chinese markets are not affected by the Indian stock markets in short run. But the result of Wald test taking Nifty as dependent variable shows that the coefficients of Chinese index taken together are not zero i.e. Chinese index effect the Indian stock market in short run. Therefore there exists a short unidirectional run causality from Chinese stock market to Indian stock market.

VII. Conclusion

The main objective of the study has been to find out the Cointegration between Indian and Chinese stock markets using the Johansen Test of Cointegration. The study employs approx. 15 years data for Nifty and Hang Seng stock indices representing the Indian and Chinese stock markets respectively. The study found bidirectional long run causal relationship between the two markets. The study also found that the Chinese markets affect Indian market in short run but it is not true vice versa. So there is unidirectional short run causality extending from Chinese to Indian stock market. An investor thus, cannot benefit by diversifying his portfolio between the two markets as the two markets move in same direction.

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