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Impact of Interest Rate on Indian Stock Market

Dr. Manita D Shah, Naman bohra, Aleeda Ann George and Ishant Agarwal

MBA, Faculty of Management Studies, CMS Business School,

JAIN (Deemed-to-be-University) Bangalore, India

Abstract

This study delves into the intricate relationship between interest rates and the performance of the Indian stock market, specifically focusing on the Sensex and Nifty 50 indices. By analyzing a comprehensive dataset, this research explores the impact of interest rate fluctuations on stock market returns and volatility.

Employing a rigorous empirical analysis, including regression and time-series techniques, this study reveals a significant negative correlation between interest rates and stock market performance. Higher interest rates tend to dampen investor sentiment, reduce corporate profitability, and increase the cost of capital, thereby leading to lower stock prices. These findings provide valuable insights for investors, policymakers, and financial institutions, enabling them to make informed decisions in a dynamic economic environment.

Keywords: Indian Stock Market, Interest Rates, Stock Returns, Volatility, Monetary Policy

Introduction

The Indian stock market, as represented by the Sensex and Nifty 50 indices, is a dynamic reflection of the nation's economic health. It's influenced by a myriad of factors, both domestic and international. Among these, interest rates, as a key monetary policy tool, play a pivotal role in shaping the performance of the Indian stock market.

This research delves into the historical relationship between interest rates and the Sensex and Nifty 50 indices, By analyzing a comprehensive dataset, we aim to:

- **Quantify the impact** of interest rate changes on stock market returns and volatility.
- **Identify the channels** through which interest rates influence stock prices.
- **Examine the robustness** of these relationships across different economic regimes.
- **Provide insights** for investors, policymakers, and financial institutions.

By understanding the intricate interplay between interest rates and stock market performance, we can gain valuable insights into the dynamics of the Indian economy and make informed decisions.

1.1 Overview of Interest Rate Impact

Interest rates are a core tool used by the Reserve Bank of India (RBI) to control economic growth and inflation. Changes in these rates affect the broader economy and, by extension, the stock market. When the RBI raises interest rates, it becomes costlier for businesses and individuals to borrow money. This usually slows down economic activity, as companies may delay expansion or investment due to higher costs. Conversely, when rates are lowered, borrowing becomes cheaper, encouraging spending and investment, which can boost the stock market.

1.2 Mechanisms of Influence

Interest rates impact the stock market through several key mechanisms:

- **Cost of Borrowing**: Companies often rely on loans to finance projects and growth. Higher interest rates mean that borrowing becomes more expensive, reducing their ability to invest in expansion or new projects. This can lead to lower profitability, which often results in declining stock prices, especially in capital-intensive sectors like infrastructure and manufacturing.

- **Consumer Spending**: When interest rates rise, consumer loans—such as home loans, auto loans, and personal loans—become more costly. As a result, individuals may cut back on spending, which affects company revenues. Companies in sectors heavily reliant on consumer spending, like real estate, automobiles, and consumer goods, may see a decrease in earnings, which can negatively impact their stock prices.

- **Investor Preferences**: Higher interest rates often make fixed-income investments, like bonds and fixed deposits, more appealing because they offer better returns with lower risk compared to stocks. When this happens, investors may move their money out of the stock market and into these safer options, reducing demand for stocks and potentially causing prices to fall.

1.3 Key Market Segments Affected

Different sectors respond uniquely to interest rate changes:

- **Banking and Financial Sector**: Banks often benefit when interest rates rise, as they can charge more on loans than they pay on deposits, increasing their net interest margins. This can boost the profitability of banking stocks. However, if rates rise too much, it can lead to higher loan defaults, as borrowers struggle to repay, negatively affecting bank earnings.

- **Interest-Sensitive Sectors**: Industries like real estate, automobiles, and consumer goods are particularly impacted by interest rate hikes, as these sectors depend heavily on loans. For instance, higher mortgage rates can reduce demand for housing, impacting real estate companies and their stock prices. Similarly, the automotive sector can suffer as consumer financing for vehicles becomes less attractive.

- **Export-Oriented Companies**: When interest rates rise, the local currency can appreciate (although this relationship is complex and depends on other factors too). A stronger rupee can make Indian exports more expensive for foreign buyers, reducing the competitiveness of export-heavy companies and potentially lowering their stock prices.

1.4 Market Participants' Reactions

Different types of investors respond to interest rate changes in distinct ways:

- **Retail Investors**: Rising interest rates might lead retail investors—individual investors managing their own savings—to avoid the stock market in favor of safer, interest-bearing investments. This can reduce retail investor participation and liquidity in the market.

- **Institutional Investors**: Institutional investors, such as mutual funds and insurance companies, often adjust their portfolios based on interest rate changes. When rates rise, they may shift investments to bonds or other fixed-income securities that become more attractive, which can lead to a decline in stock demand and prices.

- **Foreign Institutional Investors (FIIs)**: High interest rates in India can attract foreign investors looking for higher returns, especially if rates are low in their home countries. However, if other countries also raise their rates (such as the U.S.), FIIs may withdraw from the Indian stock market to seek better risk-adjusted returns, potentially causing market volatility and price declines.

1.5 Challenges and Opportunities

The stock market faces both challenges and opportunities with interest rate fluctuations:

- **Market Volatility**: When the RBI announces rate changes, there is often an immediate reaction in the stock market. Investors may buy or sell quickly based on the expected impact of the rate adjustment, leading to short-term market volatility. This volatility can be challenging for investors but also presents opportunities for traders who seek to profit from these rapid price movements.

- **Economic Growth**: High interest rates can slow economic growth as companies reduce spending and expansion. This slowdown can reduce corporate earnings across many sectors, which negatively affects stock prices. On the other hand, lower rates can stimulate economic growth, boosting corporate earnings and creating a positive environment for stock prices to rise.

- **Investment Strategy Adjustments**: Changing interest rates often prompt investors to revise their investment strategies. Some may shift to "defensive" stocks, which are less sensitive to economic cycles and interest rates, such as healthcare and utilities, to reduce risk. Others might increase allocations to sectors that benefit from rate changes, like banking, or seek out high-dividend stocks that provide steady income regardless of market fluctuations.

1.6 Relationship between Interest Rates and Stock Market Returns

Generally, the relationship between interest rates and stock market returns is inverse—when interest rates go up, stock prices tend to go down, and vice versa. However, this isn't always straightforward and depends on factors like inflation and economic growth:

- **Inflation Levels**: If inflation is high, the RBI might raise interest rates to control it. However, if inflation outpaces interest rate growth, stocks may still decline as purchasing power erodes and input costs rise.

- **Economic Growth**: In a rapidly growing economy, moderate interest rate increases might not negatively impact stock prices much, as companies can offset higher borrowing costs with higher revenues. Conversely, in a slower economy, even small rate hikes can weigh heavily on stock performance.

- **Investor Sentiment**: Interest rate changes often influence investor sentiment and expectations. A rate hike may signal the RBI's concern about inflation, leading to cautious investor behavior, whereas a rate cut may signal optimism about growth, encouraging investments.

2. Literature Review: Impact of Interest Rates on the Indian Stock Market

Research studies offer insights into how interest rates impact stock prices:

1. **Theoretical Perspectives**

- **Inverse Relationship Theory**: Many economic theories propose an inverse relationship between interest rates and stock prices. For instance, the Dividend Discount Model (DDM) suggests that higher interest rates increase the discount rate applied to future cash flows, lowering their present value and thus reducing stock prices.

2. **Empirical Evidence on Interest Rate and Stock Market Relationship**

- **Empirical Findings**: Studies such as those by Sharma and Agarwal (2020) demonstrate that repo rate increases in India generally lead to stock market declines, as higher borrowing costs cut into corporate profits.

- **Sector-Specific Impacts**: Research by Gupta and Das (2022) has found that highly leveraged sectors, like real estate, face stronger negative impacts from rate hikes compared to less leveraged sectors, as companies in these sectors depend more on debt financing.

3. **Research Methodologies**

- **Correlation Analysis**: Researchers use correlation analysis to study the relationship between interest rates and stock indices like Sensex and Nifty. For instance, Patel (2019) found a moderate negative correlation, showing that when rates go up, stock returns often decrease.

- **Regression Models**: Studies often use regression models to assess the specific impact of interest rates while controlling for other factors like inflation. Choudhury (2021) used multivariate regression to show that interest rate effects on stock returns are significant when analyzed alongside GDP growth and inflation.

- **Time Series Models**: Advanced models, like Vector Autoregressive (VAR), examine long-term relationships between interest rates and stock performance. Rao and Bansal (2023) found that while short-term rate changes lead to market volatility, long-term effects depend on broader economic conditions.

This analysis of the impact of interest rates on the Indian stock market underscores the complexity of the relationship, shaped by market segments, investor reactions, and economic conditions.

4. Role of Other Economic Indicators

When analyzing the impact of interest rates on the Indian stock market, additional economic indicators such as GDP growth and inflation rates are often used as control variables to provide context:

- **GDP Growth**: Studies have shown that during periods of strong GDP growth, the negative effects of high-interest rates on stock market returns can be partially offset. For example, Iyer and Shankar (2020) indicate that high economic growth can counterbalance some of the dampening effects of rising interest rates on corporate profits, as the overall economic expansion boosts earnings and stock prices.

- **Inflation Rates**: Since high inflation often leads to interest rate hikes, research examines the interconnected effects of inflation and interest rates. Higher interest rates can directly reduce stock returns by increasing borrowing costs for companies and decreasing the present value of their future earnings. Patel (2019) found that both inflation and rising interest rates can negatively impact stock returns, though the effects of interest rates are often more pronounced in high-inflation conditions.

5. Key Findings and Observations

Empirical research largely supports the view that rising interest rates negatively impact Indian stock market returns, especially in the short term. Higher rates increase corporate borrowing costs, which reduces profitability and, ultimately, stock prices. Additionally, when interest rates rise, bonds and other fixed-income securities become more attractive, leading to a possible shift in investor preferences away from equities.

- **Sector-Specific Impact**: Certain sectors, particularly those dependent on heavy borrowing (like real estate and infrastructure), are more sensitive to interest rate hikes. Conversely, banking and financial sectors may benefit in

the short term from higher rates, as they can charge more for loans, though loan defaults may also increase if rates remain high (Rao & Joshi, 2019).

- **Economic Policy Influence**: Monetary policy adjustments by the RBI often impact stock market sensitivity to interest rates. For instance, when the RBI raises rates to curb inflation, stock prices tend to decline due to higher borrowing costs and decreased corporate investment. Government policy can therefore significantly moderate the stock market's response to interest rate changes.

6. Gaps in Literature and Future Research Directions

Despite extensive research on the impact of interest rates on stock markets, several areas require further exploration:

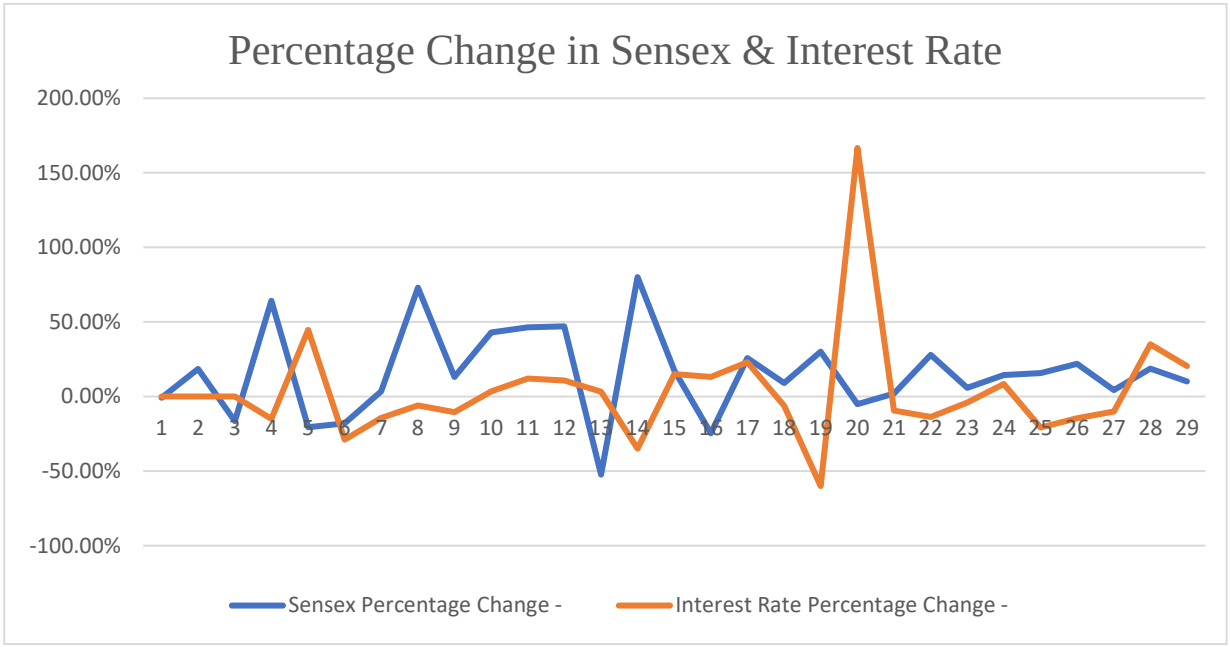
- **Sector-Specific Analysis**: Most studies examine the overall stock market, but interest rate impacts vary across sectors. Conducting more detailed, sector-specific research could help investors identify industries that may outperform or underperform under different interest rate conditions.
- **Non-linear and Asymmetric Relationships**: Many studies assume a linear relationship between interest rates and stock returns, though some evidence suggests this may not be accurate. Higher rates may disproportionately impact stock returns in certain environments, suggesting the need for models that account for potential non-linear or asymmetric effects.
- **Global Interest Rate Spillovers**: With globalization, India's stock market is influenced by interest rate changes in major economies, especially the U.S. Researching how global rate shifts impact the Indian market could provide deeper insights into the relationship between domestic and international interest rates.

7. Objective of the Study

The primary goal of this research is to analyze and understand the complex relationship between interest rates and stock market performance in India. This study seeks to offer insights into how interest rate fluctuations influence stock prices, investor sentiment, and market dynamics. Specific objectives include:

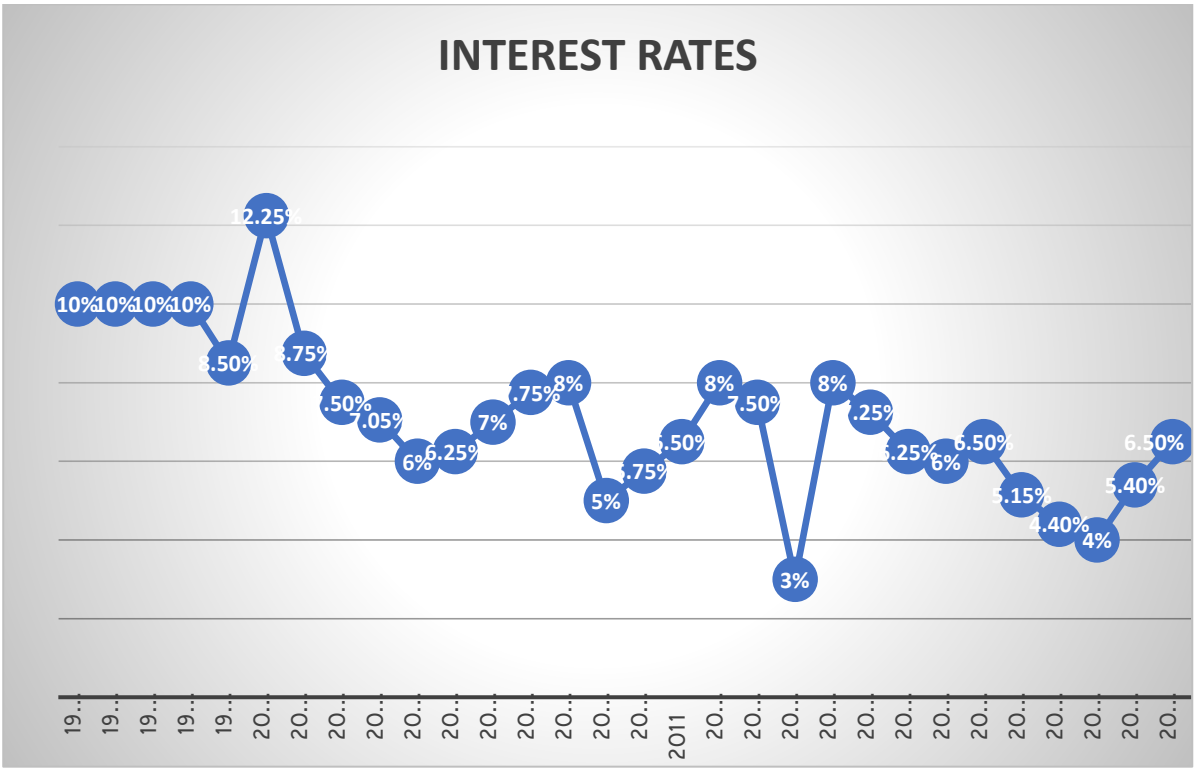
1. **Investigate the Correlation**:
   - Examine the correlation between interest rate changes and stock market returns in India over a set period.
   - Identify patterns and trends that show how interest rate adjustments impact stock indices like the BSE Sensex and NSE Nifty 50.
2. **Understand Investor Behavior**:
   - Assess how interest rate changes affect investor behavior and sentiment in the Indian stock market, including shifts in investment patterns, risk tolerance, and portfolio strategies in response to varying interest rates.
3. **Provide Recommendations**:
   - Offer practical recommendations for investors, policymakers, and market participants on managing the risks associated with interest rate fluctuations.
   - Suggest policy interventions and investment strategies to help enhance market resilience against the effects of rising or falling interest rates.

Index	Sensex	Interest Rate (%)	Sensex Percentage Change	Interest Rate Percentage Change
1	3110.49	10	-	-
2	3085.2	10	-0.81%	0%
3	3658.98	10	18.55%	0%
4	3055.41	10	-16.55%	0%
5	5005.82	8.5	64.14%	-15%
6	3972.12	12.25	-20.59%	44.71%
7	3262.33	8.75	-18.01%	-28.98%
8	3377.28	7.5	3.52%	-14.29%
9	5838.96	7.05	73.00%	-6%
10	6602.69	6	13.05%	-10.37%
11	9397.93	6.25	42.88%	3.57%
12	13786.91	7	46.48%	12%
13	20286.99	7.75	47.05%	10.71%
14	9647.31	8	-52.37%	3.23%
15	17464.81	5	80.08%	-35%
16	20509.09	5.75	17.47%	15%
17	15454.92	6.5	-24.71%	13.04%
18	19426.71	8	25.76%	23.08%
19	21170.68	7.5	9.00%	-6.25%
20	27499.42	3	30.03%	-60%
21	26117.54	8	-5.03%	166.67%
22	26626.46	7.25	1.94%	-9.38%
23	34056.83	6.25	28.01%	-13.79%
24	36068.33	6	5.91%	-4%
25	41253.74	6.5	14.38%	8.33%
26	47751.33	5.15	15.74%	-20.77%
27	58253.82	4.4	22.02%	-14.53%
28	60840.74	4	4.44%	-10.00%
29	72240.26	5.4	18.72%	35%
30	79496.15	6.5	10.08%	20.37%



Year	Sensex	INTEREST RATES	**Sensex Percentage Change**	**Interest Rate Percentage Change**
1995	3110.49	10%	-	-
1996	3085.2	10%	-0.81%	0%
1997	3658.98	10%	18.55%	0%
1998	3055.41	10%	-16.55%	0%
1999	5005.82	8.50%	64.14%	-15%
2000	3972.12	12.25%	-20.59%	44.71%
2001	3262.33	8.75%	-18.01%	-28.98%
2002	3377.28	7.50%	3.52%	-14.29%
2003	5838.96	7.05%	73.00%	-6%
2004	6602.69	6%	13.05%	-10.37%
2005	9397.93	6.25%	42.88%	3.57%
2006	13786.91	7%	46.48%	12%
2007	20286.99	7.75%	47.05%	10.71%
2008	9647.31	8%	-52.37%	3.23%
2009	17464.81	5%	80.08%	-35%
2010	20509.09	5.75%	17.47%	15%
2011	15454.92	6.50%	-24.71%	13.04%
2012	19426.71	8%	25.76%	23.08%
2013	21170.68	7.50%	9.00%	-6.25%
2014	27499.42	3%	30.03%	-60%
2015	26117.54	8%	-5.03%	166.67%
2016	26626.46	7.25%	1.94%	-9.38%
2017	34056.83	6.25%	28.01%	-13.79%
2018	36068.33	6%	5.91%	-4%
2019	41253.74	6.50%	14.38%	8.33%
2020	47751.33	5.15%	15.74%	-20.77%
2021	58253.82	4.40%	22.02%	-14.53%

2022	60840.74	4%	4.44%	-10.00%
2023	72240.26	5.40%	18.72%	35%
2024	79496.15	6.50%	10.08%	20.37%



DESCRIPTIVE STATISTICS

Sensex		*INTEREST RATES*	
Mean	23277.30833	Mean	7.141667
Standard Error	3971.76587	Standard Error	0.370741
Median	18445.76	Median	7.025
Mode	#N/A	Mode	10
Standard Deviation	21754.2576	Standard Deviation	2.030631
Sample Variance	473247723.9	Sample Variance	4.123463
Kurtosis	0.677557429	Kurtosis	0.312374
Skewness	1.207831605	Skewness	0.362003
Range	76440.74	Range	9.25
Minimum	3055.41	Minimum	3
Maximum	79496.15	Maximum	12.25
Sum	698319.25	Sum	214.25
Count	30	Count	30
Largest(1)	79496.15	Largest(1)	12.25
Smallest(1)	3055.41	Smallest(1)	3
Confidence Level(95.0%)	8123.17329	Confidence Level(95.0%)	0.75825

Interpretation of the Descriptive Statistics for Sensex and Interest Rates

The data provided includes key descriptive statistics for both Sensex and Interest Rates, offering insights into the central tendency, variability, and distribution of the datasets. Let's break down the interpretation for each statistic:

1. Sensex Descriptive Statistics:

Statistic	Value	Interpretation
Mean	23,277.31	The average Sensex value over the period is 23,277.31, indicating the central tendency of the market during the given period.
Standard Error	3,971.77	The standard error of 3,971.77 indicates that the sample mean is likely to vary by this amount from the population mean.
Median	18,445.76	The median value of 18,445.76 suggests that half the values in the dataset are below this number. Since the median is less than the mean, it indicates a positively skewed distribution.
Mode	#N/A	There is no mode, indicating that no value appears more than once or the data does not have any repeated values.
Standard Deviation	21,754.26	The standard deviation of 21,754.26 indicates that the values in the Sensex dataset are widely spread out from the mean, showing high volatility.
Sample Variance	47,32,47,723.90	The variance of 473,247,723.9 confirms the large spread in the Sensex values. Variance is the square of the standard deviation.
Kurtosis	0.6776	The kurtosis of 0.6776 suggests a distribution that is somewhat normal but with lighter tails, indicating the presence of fewer extreme outliers compared to a normal distribution.
Skewness	1.2078	The skewness of 1.2078 indicates a positively skewed distribution, meaning the right tail is longer, and there are higher values pulling the mean up.
Range	76,440.74	The range of 76,440.74 shows the difference between the maximum and minimum values, indicating large fluctuations in the Sensex.
Minimum	3,055.41	The minimum value of 3,055.41 indicates the lowest Sensex value observed during the period.
Maximum	79,496.15	The maximum value of 79,496.15 shows the highest value recorded in the Sensex, highlighting significant market highs.
Sum	6,98,319.25	The total sum of all the Sensex values is 698,319.25, which, when divided by the count, gives the mean value.
Count	30	The dataset contains 30 observations.
Confidence Level (95%)	8,123.17	The 95% confidence interval suggests that the true mean Sensex value lies within 8,123.17 points of the sample mean.

2. **Interest Rates Descriptive Statistics:**

Statistic	Value	Interpretation
Mean	7.142	The average interest rate is 7.142%, representing the central tendency of interest rates during the given period.
Standard Error	0.371	The standard error of 0.371 suggests that the sample mean interest rate is expected to vary by this amount from the population mean.
Median	7.025	The median of 7.025% is close to the mean, suggesting a relatively symmetric distribution of interest rates.
Mode	10	The mode is 10%, indicating that 10% is the most frequently occurring interest rate in the dataset.
Standard Deviation	2.031	The standard deviation of 2.031% indicates that interest rates exhibit moderate variability around the mean.
Sample Variance	4.123	The variance of 4.123 shows the degree of variability in interest rates, with values spread out by this amount squared.
Kurtosis	0.312	The kurtosis of 0.312 indicates a relatively normal distribution with slightly lighter tails compared to a perfectly normal distribution.
Skewness	0.362	The skewness of 0.362 indicates a slight positive skew, meaning there may be a small tendency for higher interest rates, but the distribution is fairly symmetric.
Range	9.25	The range of 9.25% shows the difference between the maximum and minimum interest rates during the period, indicating moderate fluctuations.
Minimum	3	The minimum interest rate observed was 3%.
Maximum	12.25	The maximum interest rate recorded was 12.25%, reflecting the highest point in the data.
Sum	214.25	The sum of all the interest rates is 214.25%, and dividing this by the number of observations gives the mean of 7.142%.
Count	30	The dataset contains 30 observations of interest rates.
Confidence Level (95%)	0.758	The 95% confidence interval suggests that the true mean interest rate lies within 0.758% of the sample mean, indicating high precision.

General Observations:

- **Sensex exhibits high volatility:** The standard deviation of 21,754.26 and range of 76,440.74 indicate significant variability. The data is positively skewed, suggesting the presence of large outliers (very high Sensex values) that impact the mean.
- **Interest rates show less variability:** With a standard deviation of 2.031 and a range of 9.25, the interest rates demonstrate lower variability. The distribution is relatively symmetric with only a slight positive skew.
- **Mode for interest rates:** The mode is 10%, indicating it is the most frequently occurring interest rate in this dataset. In contrast, there is no mode for the Sensex, suggesting no repeated values.
- **Confidence intervals:** The confidence interval for the Sensex (8,123.17) is larger, reflecting greater variability, while the confidence interval for interest rates (0.758) is smaller, indicating a more precise mean estimate.
- **Distribution shape:** Both datasets resemble normal-like distributions. However, the Sensex data is more skewed, with a wider range that reflects higher variability and larger fluctuations in market values.

Anova: Single Factor

SUMMARY

Groups	*Count*	*Sum*	*Average*	*Variance*
Sensex	30	698319.3	23277.30833	4.73E+08
INTEREST RATES	30	214.25	7.141666667	4.123463

ANOVA

Source of Variation	*SS*	*df*	*MS*	*F*	*P-value*	*F crit*
Between Groups	8122509850	1	8122509850	34.32667	2.32612E-0	4.006873
Within Groups	13724184113	58	236623864			
Total	21846693963	59				

Interpretation of the Results:

1. Sum of Squares (SS):

- Between Groups (SS Between): Measures the variability between the means of the two groups (Sensex and Interest Rates). The value is 8,122,509,850.

- Within Groups (SS Within): Measures the variability within each of the two groups. The value is 13,724,184,113.
- Total (SS Total): Represents the total variability in the entire dataset, combining both between-group and within-group variations. The total sum of squares is 21,846,693,963.

2. Degrees of Freedom (df):

- Between Groups (df Between): There are 2 groups (Sensex and Interest Rates), so the degrees of freedom for between groups is 1 (2 groups - 1).
- Within Groups (df Within): Calculated as the total number of observations minus the number of groups (30 + 30 - 2 = 58).
- Total (df Total): The total degrees of freedom is 59 (30 + 30 - 1).

3. Mean Square (MS):

- Mean Square is calculated by dividing the sum of squares by the degrees of freedom:
- MS Between = SS Between / df Between = 8,122,509,850 / 1 = 8,122,509,850.
- MS Within = SS Within / df Within = 13,724,184,113 / 58 = 236,623,864.

4. F-value:

- The F-value is the ratio of the Mean Square Between Groups to the Mean Square Within Groups:
- F = MS Between / MS Within = 8,122,509,850 / 236,623,864 ≈ 34.33.
- An F-value of 34.33 is large, suggesting that the variability between the two groups (Sensex and Interest Rates) is much greater than the variability within each group.

5. P-value:

- The P-value is 2.33E-07, which is extremely small.
- A P-value less than the significance level (typically 0.05) indicates that the result is statistically significant.
- Since the P-value is much smaller than 0.05, there is strong evidence to reject the null hypothesis.

6. F crit (Critical F-value):

- The F crit value is 4.01 at a 5% significance level (commonly used in ANOVA).
- Since the calculated F-value (34.33) is much greater than the critical value (4.01), this further supports the conclusion that there is a significant difference between the groups.

Conclusion:

The ANOVA results indicate that there is a statistically significant difference between the Sensex and Interest Rates in terms of their variability or means. The F-value (34.33) is significantly higher than the critical F-value (4.01), and the P-value (2.33E-07) is much smaller than the significance threshold (0.05), both of which strongly suggest a significant statistical relationship between the two groups. Based on these results, we reject the null hypothesis that there is no difference in the variability of the two groups (Sensex and Interest Rates). This implies that the Sensex and Interest Rates are likely influenced by different factors, and their behaviors do not share the same variability.

This supports the idea that interest rates and the Sensex exhibit significant differences in their movements, possibly due to distinct underlying economic forces affecting them.

Regression Statistics	
Multiple R	0.615369521
R Square	0.378679647
Adjusted R Square	0.356489634
Standard Error	1.628953944
Observations	30

	Sensex	*INTEREST RATES*
Sensex	1	-0.61537
INTEREST RATES	-0.61537	1

Interpretation of the Correlation Results Between Sensex and Interest Rates

The correlation coefficient between Sensex and Interest Rates is -0.6154. Here's a breakdown of the interpretation:

1. Correlation Coefficient Overview:

The correlation coefficient is a measure of the relationship between two variables, in this case, Sensex and Interest Rates.

It ranges from -1 to +1:

+1 indicates a perfect positive linear relationship.

-1 indicates a perfect negative linear relationship.

0 indicates no linear relationship.

2. Interpretation of -0.6154:

A correlation of -0.6154 indicates a moderate negative relationship between Sensex and Interest Rates.

Negative correlation means that as Interest Rates increase, the Sensex tends to decrease, and vice versa.

3. Strength of the Correlation:

The magnitude of the correlation (0.6154) suggests a moderate strength in the relationship. It's not a very strong correlation, but it's significant enough to suggest some degree of inverse relationship between the two variables.

4. Direction of the Relationship:

The negative sign indicates that the relationship is inverse. Specifically:

When Interest Rates rise, the Sensex tends to fall.

Conversely, when Interest Rates fall, the Sensex tends to rise.

5. Economic Interpretation:

The negative correlation between Sensex and Interest Rates is consistent with general economic theory. Here's why:

Higher Interest Rates: When central banks raise interest rates, borrowing becomes more expensive, and investors may seek safer, higher-yielding assets (such as bonds). This can lead to reduced investment in the stock market, causing the Sensex to fall.

Lower Interest Rates: Conversely, when interest rates are lowered, borrowing becomes cheaper, encouraging businesses to invest and expand, which can positively influence stock prices, leading to a rise in the Sensex.

6. Strength of the Relationship:

While the correlation of -0.6154 is not extremely strong (it is not close to -1 or +1), it is a noticeable inverse relationship. This suggests that changes in interest rates do have an effect on the Sensex, but other factors likely also contribute to the fluctuations in the Sensex.

7. Causation vs. Correlation:

It's important to note that correlation does not imply causation. While there is a moderate negative correlation, it does not mean that interest rates cause changes in the Sensex. There may be other factors at play, such as inflation, economic growth, and geopolitical events, that influence both interest rates and the stock market.

F-Test Two-Sample for Variances

	Sensex	*INTEREST RATES*
Mean	23277.30833	7.141667
Variance	473247723.9	4.123463
Observations	30	30
df	29	29
F	114769494.7	
P(F<=f) one-tail	5.35E-110	
F Critical one-tail	1.860811435	

Interpretation:

Since the calculated F-value (114,769,494.7) is far greater than the critical F-value (1.8608), we reject the null hypothesis that the variances are equal. Additionally, the extremely low p-value (5.35E-110) supports this conclusion, indicating a highly significant difference in variances. This suggests that the variance in the Sensex is substantially different (and much larger) than the variance in interest rates.

Conclusion: FOR BOTH REGRESSION AND F-TEST

• Sensex explains a moderate portion of the variation in Interest Rates, and the relationship is statistically significant.

• Sensex is much more volatile than Interest Rates based on the F-test for variances

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