THE INDIAN STOCK MARKET AND POLITICAL CYCLES

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ABSTRACT

We examine the relationship between the Indian stock market and political cycles over the period of October 1999 to April 2019. First, we find Indian stock market returns are not statistically different during periods when the prime minister is from the left-leaning Indian National Congress or from the right-leaning Bharatiya Janata Party. Second, we find Indian stock market returns during any one particular year are not statistically different from other four years of the five-year Indian prime ministerial term. Third, we find Indian stock market generate high positive returns comparable to that of the U.S. stock market irrespective of political affiliation of the prime minister and the ruling party of the Indian government. We conclude Indian stock market generates high positive returns regardless if the control of the government is with the Indian National Congress or the Bharatiya Janata Party.

Keywords: *Indian stock market, political cycles. Prime minister of India, Bharatiya Janata Party, Indian National Congress, Democrat premium, left-wing premium, presidential cycles, election cycles.*

1. INTRODUCTION

Since early 1990s, the Indian government has pursued significant liberalization policies to increase private and foreign investment. The Indian stock market is widely considered an important investment destination for international investors in recent years. At over 1.3 billion people, India has the second largest population in the world, a large diverse population comprising many religions, ethnicities, languages, etc. with political election cycles uniquely different from that of the United States. India has elected political leaders democratically since its independence in 1947. In recent decades, Indian politicians have increasingly pursued economic policies that are supportive of economic development irrespective of their political party affiliations. International investors are increasingly interested and bullish about investing in the Indian stock market. However, there appears some apprehension on how Indian election outcomes and changes in political leadership would affect its stock market and the overall economy. It is for this reason we believe that there is a need to investigate how the changes in political cycles affects the Indian stock market.

Researchers have extensively investigated the relationship of U.S. political party affiliation with the U.S. stock market returns. These researchers' state U.S. stock market generate different returns during Democratic versus Republican presidential terms because of different fiscal policy pursued by each political party. These researchers have generally found that U.S. stock market returns are significantly higher during the second half (i.e. years 3 and 4) than the first half (years 1 and 2) of U.S. presidential terms irrespective of political party affiliation. Subsequently, some researchers have investigated the relationship of political party affiliation and stock market in other countries as that found in the United States. We conduct similar investigations in the case of India.

The Indian constitution follows a parliamentary political system. As per the Indian constitution, the prime minister is the chief executive of the government of India. The prime minister is the elected leader of the political party that has the majority in the Lok Sabha, the lower house of the Indian parliament. The members of the Lok Sabha referred as the members of the parliament (MPs) represent different states constituencies of the country. These members of the parliament subsequently vote to elect the prime minister of India. The political structure in India is, however, more complex than in the U.S. It has many