National University of Science and Technology

Think in Other Terms

FACULTY OF COMMERCE

DEPARTMENT OF BANKING

AN ANALYSIS OF THE EFFECT OF MONETARY POLICY ON STOCK MARKET PERFORMANCE IN ZIMBABWE (2003-2007)

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ABSTRACT

From 1997, Zimbabwe was experiencing an economic recession and yet the Zimbabwe Stock Exchange has been on an upward trend defying theoretical literature that says the stock market is a barometer of a country's economic performance. This drew the attention of the researcher to analyze how changes in monetary policy variables have affected the returns on the stock market in Zimbabwe. It was carried out for the period stretching from 2003 to 2007. Various findings by different authors were reviewed pertaining to the topic and the different variables used. The study was targeted at individual investors with other interested parties being stock market analysts, economic analysts, stockbrokers and fund managers. Causal research was the research design method used as well as exploratory research through the formulation of a hypothesis was also used in this research. The study was targeted at individual investors with other interested parties being stock market analysts, economic analysts, stockbrokers and fund managers. Sampling techniques used were judgmental and systematic random sampling. Data was collected through interviews and questionnaires. A multiple linear regression model was run to analyze the effect of monetary policy changes on stock market returns. For stock market returns, the industrial index was used while the monetary policy variables considered were money supply, interest rates, and the exchange rate. Inflation was considered as the forth variable as it is strongly linked to the monetary policy and other variables. Regression analysis through the use of a software program, Minitab, established that there is a positive relationship between all monetary policy variables and stock returns. Factors other than these contributed negatively to stock returns. Conclusions drawn by previous researchers were that there is a negative relationship between stock returns and interest rates. This was not the case in Zimbabwe because even though interest rates were increasing, stock returns kept increasing as well. The researcher's findings for inflation, money supply growth and the exchange rate were in line with other researchers' findings. Investor appetite increased on the stock market as it was the only investing ground that yielded positive returns in real terms and retained the ever eroding value of money in Zimbabwe for the period under review. Such divergence from theory was due to the abnormal economic environment that was characterized by hyperinflation and the frequent printing of money. An expansionary monetary policy therefore leads not only to inflation but an increase in stock market returns. Thus the research concluded that if monetary policy variables are increased under a hyperinflationary environment, stock market returns will also increase. The researcher recommended the implementation of an expansionary monetary policy backed with production to the central bank and the establishment of commodities, bond and derivatives markets in Zimbabwe. The researcher suggested that future researchers analyze the level of contribution to GDP due to the effect of monetary policy changes on the ZSE.