NEPAL'S EXTANT OBSERVATION: FOSTERING CAPITAL MARKETS FOR ECONOMIC GROWTH

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DOI: 10.5958/2278-4853.2022.00015.5

ABSTRACT

The objective of this research is to delve at how to foster a capital market for economic growth in Nepal, as well as a situational analysis of the country. The capital market makes a substantial contribution to the growth of the national economy by allowing investors' funds to invest as possible opportunities and saving funds to be mobilized and distributed to users. By issuing shares, debentures, and bonds for business organizations, the capital markets provide an effective means of sourcing long-term finances, while also providing an investment opportunity for people and institutions. In recent decades, the Nepalese capital market has been developing and strengthening. The study's aims to look at the e
volution of the capital market, as well as the capital market's contribution to financial resources, economic growth, and GDP. This research period spans the years 1993 through 2019. The basic regression model has been used to estimate the economic impact of the capital market on the economy. Using secondary data, a descriptive and analytical study approach has been applied. The findings show that the capital market has made a major contribution to financial resource mobilization, economic growth, and GDP. The Nepalese financial markets should be systematized and updated, as per this study.

KEYWORDS: C*apital Market, Financial Resources, Mobilization, Impact, Economic Growth, Nepalese Economy, JEL Code: E44, 016.*

INTRODUCTION

Capital market is defined as the stock as well as share market that mobilizes financial resources for economic development and the economic symbols of any economy. This market plays a vital role of an economy which allows investor's fund to gorge potential opportunity such as saving funds are mobilize and channeled efficiently to users. Levine and Zeros (1998) **[1]** remarked that capital market is expected to encourage savings by providing individuals with an extra financial instrument which can better meet their risk preferences and liquidity needs. King and Levine

(1993) **[2]** highlighted that financial resources is a good predictor for economic growth, capital accumulation and productivity.

Bolbol et al. (2005) **[3]** pointed that capital market development had a positive impact on economic growth. Niewwerburgh (2006) [**4]** stated that economic growth is the main caused of capital development of the economy. Thus, capital market is assumed to be the barometer of the economy by which we can know the economic conditions of the country. Adhikari (2004) **[5]** remarked that capital markets provide an effective way of procuring long-term funds by issuing shares, debentures and bonds for corporate enterprises and government which also provides an investment opportunity for individuals and institutions.

Capital market supports to the flow of non-productive small savings spread among the people to the productive sector through resources mobilization. These market linkages working relationships between people engaged in saving, mobilization and investment capital. Besides this, capital market plays a contributory role in the economy whereas it mobilizes the unproductive financial resources in the productive sectors of the economy (NRB, 2012) **[6].**

Nepalese primary capital market initiated after 1937 when Biratnagar Jute Mill and Nepal Bank Limited started the primary issue of shares and the secondary capital market started after the establishment of the regulator of Securities Board of Nepal (SEBON) and Nepal Stock Exchange Ltd. (NEPSE). The capital market is a situation which promotes the buying and selling of debt or equity securities that aids economic growth by mobilizing the savings of the economic sectors and directing towards channels of productive mobilization.

Sharpa et al (1998) **[7]** pointed that the securities market is a mechanism which created to facilitate the exchange the financial securities as well as assets bringing together buyers and sellers of the securities. After the establishment of the NEPSE, the sole stock exchange of Nepal opened an avenue for investors both small and large investment in enterprises operating in different sectors. It also provided enterprises with an opportunity to obtain capital that is indispensable to any business. SEBON is the regulator of securities market which has been regulating the securities market under the Securities Act (2006).

For international standardization of capital market, SEBON has got membership to the International Organization of Securities Commissions (IOSCO) which is the international body that brings together the world's securities regulators and recognized as the global standard setter for the securities sector to create a market of international standards as well as adopting or replacing the current local-based online trading system by a tested international standard online software system. To make the secondary market more competitive and wide-reacting, subsidiary companies of commercial banks with countrywide networks, immediately licensed to functions as a share trading Broker Company.

However, modernization of the capital market was started after 2016 as of the three important functions like trading, ownership transfer and payment settlement of the secondary market while share trading was automated in 2007, leaving the other functions to sty manual. The three functions were automated with the introduction of the paperless trading system in January 2016, which was introduced in the Nepalese capital market to new era of modernization, building this market as the fifth in South Asia.

The well-developed capital markets are a driver of economic growth where it yields positive effects on employment. From the investors' side, capital markets create investment environment and risk management tools (World Bank Group, 2020) **[8].**

The existing scenery of capital market of Nepal is the growing phase but not playing the significant role for mobilization. If the Nepalese capital market is systematically managed and developed, it can be a source of the much needed capital necessary for economic growth. The supply of capital is frequently required to maintain the momentum of the growth in GDP. The organized and systematic capital market could serve as the medium for transferring part of the business ownership of foreign corporations to the citizens.

The Nepalese capital market is highly influenced by non-economic parameters such as social, political, ethical as well as other factors. The capital market supports to mobilize the surplus unit to deficit for productive investments and mobilize the scattered resources and channels them into productive sectors. Capital market is also assumed to an effective instrument for expanding productive capacities of the country. In the context of Nepal, despite the past history of decade of planned economic activities to develop real sector of a country, little attention was paid to the development of capital market.

LITERATURE REVIEW

This sector reviews the different research studies toward the capital market which have been published domestically and internationally. Ujunwa and Mode be (2012) **[9]** stated that capital market is one of the most vital areas of the economy which provides companies access to capital and investors with a slice of ownership in the economy and the potential of gains based on company's future performance. The capital markets are a vital part of the financial development and economic development of a country. Development of the capital market has been directly linked with the economic growth and resources mobilization. This market plays a significant role in mobilization of domestic resources and channeling them effectively to raise economic production and productivity. Besides this, the development of capital market is taken as a key determinant of the country's level of savings, efficiency and investment and ultimately its rate of economic growth.

Torres, Wellsand Khan (2013) **[10]** studied the impact of reforms of capital market on economic development in Latin American countries. They applied market capitalization, value traded and capital raised for measuring capital market development. The researchers applied annual inflation rate and ratio of government deficit to GDP as the alternative indicators. Obiakor and Okwu (2011) [**11**] examined the relevant indicators of economic growth and performance of capital market like GDP, market capitalization value of shares traded foreign private investment and gross capital formation. They found that development of capital market has a positive relation with economic growth whereas the economic growth which could be defined as the capital market development.

The capital market plays a vital role in mobilization of domestic resources and channeling them effectively to raise economic production and productivity. The level of capital market development is assumed to be an important determinant of a nation's level of savings, efficiency and investment ultimately its rate of economic growth (Buyuksal varci & Abdiglu, 2011) **[12].** Dudley and Hubbard (2004) **[13]** remarked that development of stock market reflects the development of capital market. By linking equity market with the development of capital showed a positive impact. Debt and equity markets supports allocate capital in an economy.

Levine and Zervos (1997) [**1**] examined the relationship between economic growth and stock development where they found a strong positive correlation between the stock market development and long-run economic growth after controlling for the initial level of per capita GDP. The initial level of investment in human capital, political instability and measures of fiscal and monetary policies and exchange rate policy. They established strong linkages between stock market development and economic growth, the results does not identify a causal interaction between two variables.

Asmed (2013) introduced that capital markets are assumed to be a key indicator of national development, improving the mobilization of savings through alternative sources of financing for productive investment and supporting the development of long term savings channels. The capital markets in SAARC countries seems gradually increasing within the last 20 years where the most of members have been functioning capital markets having structures and regulations based on international best practice. Capital markets of SAARC region is varied with India being far the biggest economy. The Indian capital market has transformed with a combination of advanced information technology, strengthened regulatory structures, rapid changes of capital structures and willingness to accept foreign investment. The capital market has encouraged foreign investors and intermediaries to enter the market which led to higher standards.

World Bank (2019) **[14]** conducted empirical studies which reviewed confirm the potential benefits of capital markets to economic growth. The study finds a strong correlation between capital markets and economic growth as well capital markets development generates economic growth but the gross domestic product per capita also contributes to their capital market deepening. The empirical evidence links capital markets and innovation and developed capital markets play a key role in financing of technology.

By the examination of various research studies, it has been identified the financial sector channels savings and investments to seekers of capital and growth which constrained by credit creation in less developed financial systems. The sophisticated systems finance is viewed as responding to demand requirements and suggested that the more developed a financial system is the higher the likelihood of growth causing finance market. For the expansion and achieving the sustainable growth of economy, investor awareness and their commitment for the long-run investment play a significant role. It was expected that the awareness and commitment move in the same direction and their association contributes a lot to the economic development.

The trends of capital market of Nepal is growing phase but not playing the significant role for capital resources mobilization where the supply of capital is urgently required to maintain the momentum of the growth in GDP. The organized capital markets can serve as the medium of transferring part of the business ownership of foreign corporations to the citizens. Nepalese capital market is mostly influenced by non-economic factors like social, political, ethical and other environmental factors. The evidence speaks that capital market helps to mobilize the surplus capital to deficit unit for productive investments. It also mobilizes the scattered resources and channels them into productive sector. In the context of Nepal, though, the decade of planned economic activities to develop real sector of a country, insignificant attention was given to the development of capital market.

METHODOLOGICAL OBJECTIVES

The study's overall goal is to examine Nepal's capital market, with particular goals of examining capital market development patterns for financial resource mobilization in Nepal and observing the capital market's economic influence on GDP and NEPSE. The current study relied on secondary data to achieve these goals, and a descriptive research approach was also utilized. The essential data for the study was gathered from public sources such as the Ministry of Finance (Economic Surveys), NRB's Quarterly Economic Bulletin, SEBON's Reports, and the Nepal Stock Exchange, among others, which were the key sources of statistical information. The primary data sources were various research papers published in national and international publications, as well as national and international research reports and records. Both quantitative and qualitative methodologies have been utilized to understand and analyze the data.

The following equations are used to assess the economic impact of capital markets on macroeconomic variables: The impact of capital mobilization (CM) and share transaction (SA) on GDP is estimated by:

$$\text{Ln GDP}=\alpha_0+\beta_1 \ln CM_t+\beta_2 \ln SA_t+\varepsilon_t \ldots\ldots \textit{(i)}$$

Where ln GDP is the natural log of GDP that is affected by capital mobilization and share transactions in the capital market, ln CM is the natural log of capital mobilization, and ln SA is the natural log of share transaction in the capital market. The α_0 is constant;β_1 andβ_1 are coefficient parameters. GDP is expected to be increase due to capital mobilization and share transaction in capital market.

The impact of capital mobilization (CM)and share transaction amount (STA)on NEPSE is estimated by:

$$\ln NEPSEt = \alpha 0+ \beta_1 \ln CMt + \beta_2 \ln STAt+\varepsilon t \ldots\ldots (ii)$$

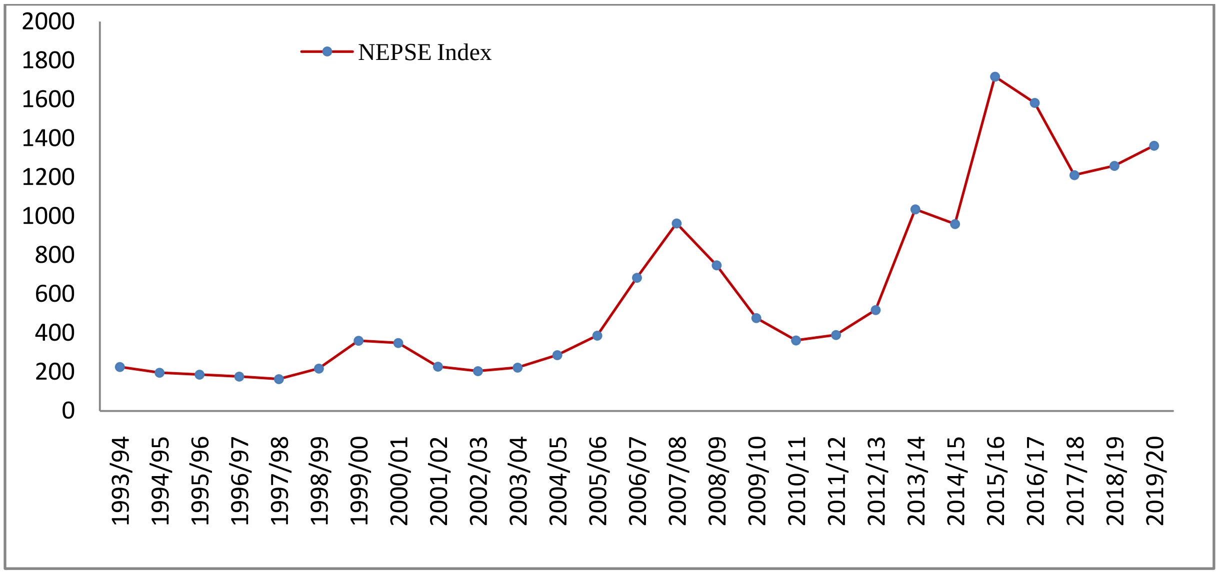
In which case, ln NEPSE is the natural log of NEPSE, and it is envisaged that capital mobilization and share transactions in the capital market would decide it. Both qualitative and quantitative factors were utilized to analyze and interpret the data obtained from various sources during the presentation and analysis phase.

The necessary econometrics, accounting, and statistical tools and methodologies have been used. Tables, graphs, and diagrams are used to convey data as needed. For multiple log linear regression estimates, SPSS software has been utilized to estimate data.

RESULTS AND DISCUSSION

Since the 1990s, Nepal's capital markets have been expanding. The primary and secondary capital markets in Nepal are expanding rapidly. The key markets are definitely seeing an increase in capital mobilization. In recent decades, the number of capital mobilizer organizations has been steadily increasing. Similarly, during the last several years, the volume of equities trading has risen. Since the 2000s, the NEPSE point value has been fluctuating. For Nepal's economic mobility, progress, and development, capital mobilization and equity transaction value play a critical role. The lowest NEPSE score was 163.30 in 1997/98, while the highest was 1718.15 in 2015/16. The contribution of market capitalization to GDP is significant. During the research period, the market capitalization of GDP ranged from 4.70 percent to 84.1 percent.

FIGURE-1: TRENDS OF NEPSE INDEX FROM 1993/94-2019/20.



Source: MOF, Economic Survey (2010/11 & 2020/21). **[15-18]**

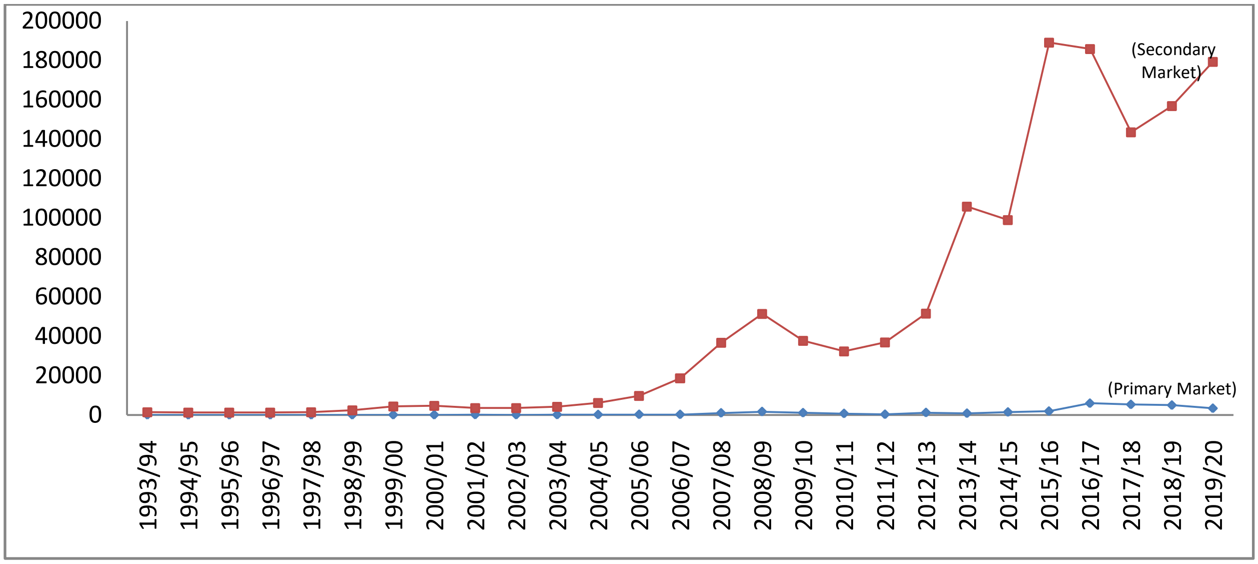
Figure 1 shows the trends of NEPSE index during the period of 1993-2019. The NEPSE index was 1377.2 points in mid-March 2020, and it had grown to 2458.5 points in mid-March 2021. This fiscal year, the stock market has performed well.

The deposit value of shares listed on the Nepal Stock Exchange has reached Rs.551.67 billion by mid-March 2021. In the previous year, these equities were worth Rs. 45.49 billion. Shares converted to Rs 46,970 million in mid-March of the 2020/21 fiscal year, which was raised through the main market. The primary market mobilized Rs.30.410 billion in the previous fiscal year's similar quarter.The initial offering of common stock raised Rs. 11.59 billion, the right stock raised Rs. 2.48 billion, bonds raised Rs. 29.60 billion, and investment trusts raised Rs. 3.30 billion during this time period. In mid-March 2020, there were 212 companies listed on Nepal, but by mid-March 2021, that number had risen to 217.

The market capitalization of in mid-March 2021 was Rs.33.73 billion, up 92.4 percent from mid-March 2020. Market capitalization as a percentage of GDP was 79.4 percent, as of mid-March in the fiscal year 2020/21. In the same time the previous year, stock transactions totaled Rs. 130.36 billion. The total number of firms registered has risen to 207. The number of registered depot members has grown to 77 as of mid-March 2020/21, offering depot services from 77 districts. The amount of dematerialized securities hit 6.2624 billion in mid-March of the 2020/21 fiscal year. In mid-March of the 2019/20 fiscal year, it was $5,206 million. Because the recipient's account is required in this problem, the number of recipient's account openings has skyrocketed.

FIGURE 2: CAPITAL MOBILIZATION IN PRIMARY MARKET AND SHARE TRANSACTION OF SECONDARY MARKET

(Rs. in Ten Million)



Source: Economic Surveys 2010/11 & 2020/21. **[19]**

Figure 2 depicts the status of capital mobilization in the primary market and the volume of share transactions in the secondary market. The quantity of share transition in the secondary market is larger in the studied periods as compared to capital mobilization in the primary market. Both of these figures are on the rise.

Figure-3: Market Capitalization to GDP (%) from 1993/94-2019/20

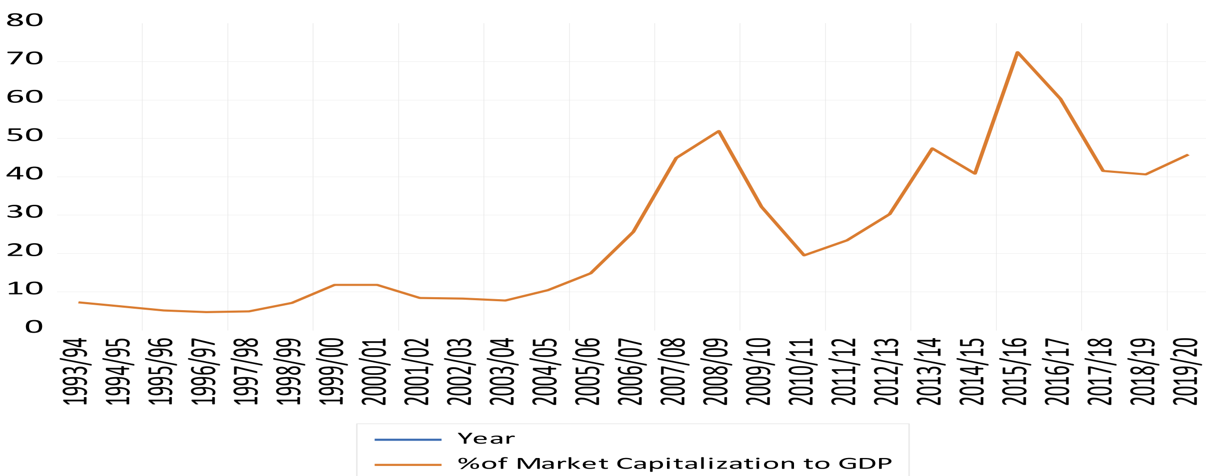


Figure 3 depicts the variations in market capitalization to GDP over the period of 1993-2019. During the study period, the contribution of market capitalization to GDP appears to rise and fall at distinct time intervals. In the initial periods, the market capitalization to GDP showed increasing trends where it reached to peak level in 2008/09 then it started to fall which reached at the bottom level in 2010/11. After 2010/11, it again started to rise where it was highest in 2016/17 then it started to falling trends.

Impact of Capital Mobilization in GDP

The purpose of this research is to determine the impact of capital mobilization and stock market transactions on GDP. According to this study, increased capital mobilization and share transactions in the capital market have a favorable impact on GDP. Capital mobilization and share transactions have made a substantial contribution to GDP. Capital mobilization and share transactions have dictated the value of GDP. Capital mobilization and share transactions have a beneficial influence on GDP, according to empirical research.

Equation Analysis

The log linear multiple regression analysis examines the function of independent variables in relation to a specific dependent variable in order to see how a percentage change in one variable affects the anticipated percentage change in the other. This analysis indicates that the link between capital mobilization and share transactions and GDP in Table-3 using data from 1993/94 through 2019/20.

$$\ln GDP=\alpha_0+\beta_1 \ln CM_t+\beta_2 \ln SA_t+\varepsilon_t$$

$$\ln GDP=3.6604+ 0.2790 \ln CM_t+ 0.2014 \ln SA_t+\varepsilon_t$$

TABLE 3: REGRESSION BETWEEN CAPITAL MOBILIZATION AND GDP

Regression Statistics					
Multiple R	**R Square**	**Adjusted R-Square**	**Standard Error**	**Observations**	
0.958332629	0.918401428	0.911601547	0.126869746	27	
ANOVA					
	df	***SS***	***MS***	***F***	***Significance F***
Regression	2	4.3478782	2.1739391	135.0613971	8.71346E- 25
Residual	24	0.3863023	0.0160959		
Total	26	4.7341806			
	Coefficients	***Standard Error***	***t Stat***	***P-value***	***Lower 95%***
Intercept	3.6604759	0.08073517	45.3392965	9.04242E-25	3.4938467
Natural Log of Capital Mobilization	0.2790231	0.0890039	3.13495392	0.00449371	0.0953281
Natural Log of Share Transaction	0.2014003	0.0760640	2.64777208	0.01409157	0.0444117

Source: Authors Computation.

The relation between capital mobilization and GDP has been examined using regression analysis. Using data from 1993/94 to 2019/20, the natural log of capital mobilization and the natural log of GDP were regressed on the natural log of capital mobilization to investigate the link between capital mobilization and GDP. Because the entire link is statistically significant (p value less than

5% which is 8.71346E- 25), the regression fits (R^2 = 0.9184).It demonstrates that the variance in the total explanatory variables accounts for 91.84 percent of the variation in GDP.

Similarly, with p = 8.71346E-25, there is a significant relationship between share transactions and GDP. The conclusion seemed to be correct because all diagnostic parameters supported the link, such as the regression coefficient being significant at a 5% p value. According to the coefficients, a 1% increase in capital mobilization raises GDP by 0.279 percent. In the same way, a 1% rise in share transactions boosts GDP by 0.201 percent. It shows that capital mobilization and share transactions have a favorable influence on Nepal's GDP.

Impact of Capital Mobilization and Share Transaction on NEPSE Index

Capital mobilization and share transactions on the capital market have a crucial role in determining the NEPSE Index. Essentially, the amount of a share transaction determines the value of a NEPSE point. The quantity of a share transaction has a favorable influence on the NEPSE index, according to empirical research. Table 4 shows that the association between share transaction amount and NEPSE index is positive using data from 1993/94 through 2019/20.

$$\ln NEPSE_t = \alpha_0 + \beta_1 \ln CM_t + \beta_2 \ln STA_t + \varepsilon_t$$

$$\ln NEPSE_t = 3.921 + 0.021 \ln CM_t + 0.319 \ln STA_t + \varepsilon_t$$

TABLE 4: REGRESSIONOF CAPITAL MOBILIZATION & SHARE TRANSACTION ON NEPSE INDEX

,*Regression Statistics*					
Multiple R	**R Square**	**Adjusted R Square**	**Standard Error**	**Observations**	
0.959533957	0.920705414	0.914097532	0.011000903	27	
ANOVA					
	df	***SS***	***MS***	***F***	***Significance F***
Regression	2	0.033724466	0.016862233	139.3344171	6.17906E-14
Residual	24	0.002904477	0.00012102		
Total	26	0.036628943			
	Coefficients	***Standard Error***	***t Stat***	***P-value***	***Lower 95%***
Intercept	0.579432056	0.007000564	82.76933574	5.28999E-31	0.564983602
Natural Log of Capital Mobilization	0.025427507	0.007717548	3.294765025	0.003050618	0.009499271
Natural Log of Share Transaction	0.017003237	0.006595532	2.577993195	0.016504085	0.003390728

Source: Authors Computation.

The relation between the share transaction and the NEPSE Index was investigated in the regression analysis. The natural log of the NEPSE Index was regressed on the natural log of share transaction using data from 1993/93 to 2019/20 to examine the link between share transaction and the NEPSE Index. Because the total link is statistically significant with a p-value less than 5%, the regression fits (R2=0.9207) (6.17906E-14). It means that the variance in the supplied total explanatory factors explains 92.07 percent of the variation in the NEPSE Index.

However, at p = 6.17906E-14, the connection between capital mobilization and the NEPSE Index is negligible. The finding seemed to be incorrect because all diagnostic criteria supported the link, such as the regression coefficient being insignificant at a p-value of 5%. According to the equations, a 1% increase in capital mobilization raises the NEPSE Index by 0.025 percent. The NEPSE Index rises by 0.017 percent for every 1% increase in share transactions. It shows that capital mobilization and share transactions have a favorable influence on Nepal's NEPSE Index.

CONCLUSIONS

The function of capital markets in mobilizing financial resources is critical. The economic underpinnings of economic development determine the liquidity of financial capital. The liquidity of a country's market is increased via capital markets. Nepal's capital markets are still in their infancy. Strong disclosure enforcement, possibly infeasible domestic markets, imperfect regulatory structures, and inadequate disclosure by the Limited Company all contributed to the Limited Company's lack of transparency. A state stock exchange system that has not been upgraded, as well as a market that has not been properly modernized, exist. **[20, 21]**

As indicated in the strategy authorized by SEBON and the program to decrease monopolistic circumstances, capital markets are pursuing independent exchanges in the corporate and private sectors. In terms of day-to-day stock trading, the modern stock market has the ability to make significant progress.The NEPSE index could not be a reflection or indication of the actual economy because the real sector does not appear to play a significant role. Capital mobilization and equity trading, on the other hand, have a favorable influence on Nepal's NEPSE index and GDP, according to this study. **[22]**

The actual sector contribution is roughly 1%, according to Nepal's index and economic development data for the previous two decades. Various actions must be done to boost business enterprises in the capital markets, including considerable tax cuts, adding industries to the central bank's priority list, and creating an international free pricing system.Economic development and reform are required for capital market modernization, and the government must use economic stimulus to restore the ailing economy. The stability and comprehensive modernization of Nepal's capital markets will be determined by the rate of economic recovery and structural changes.

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