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GENERAL ELECTIONS AND THE STOCK MARKET

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Introduction

India holds general elections every five years to elect representatives for the Lok Sabha, ultimately determining the Prime Minister. These recurrent elections significantly impact the political landscape and investment environment, influencing economic policies, regulatory frameworks, and sectoral dynamics. Indian elections are riddled with far-reaching consequences, with their effects not only limiting themselves to the political landscape but also marginally affecting the stock market and economy. Uncertainty is ubiquitous; ranging from the common sundry labourer to the most accomplished business, a sense of unease underlines the election period.

The volatility caused to stock market performance remains the primary anxiety for the market participants, analysts, and policymakers, and there is a certain element of **political risk** associated within the psyche of potential stakeholders. The relation between political risk and the capital market is not so significant in the long term although it does affect the market in the short term as it dries out quickly soon after the election result is announced. The election result primarily **increases the volatility** in the market for a few days. Studies have found that the highest average return occurred once the result was announced and subsequently settled down in a few days. A spike of variability was observed in the next seven days period after the election result announcement. **It has been observed that the pre-election period usually gets more affected than the post-election period**.

Political transitions can trigger substantial changes in government policies, economic priorities, and regulations, subsequently affecting various sectors of the economy and companies, the purpose of this paper is to highlight the actual impact of general elections on the stock market. In many instances, the market only substantially fluctuates as a result of political announcements such as law amendments, regulation promulgation, and national elections. However, while

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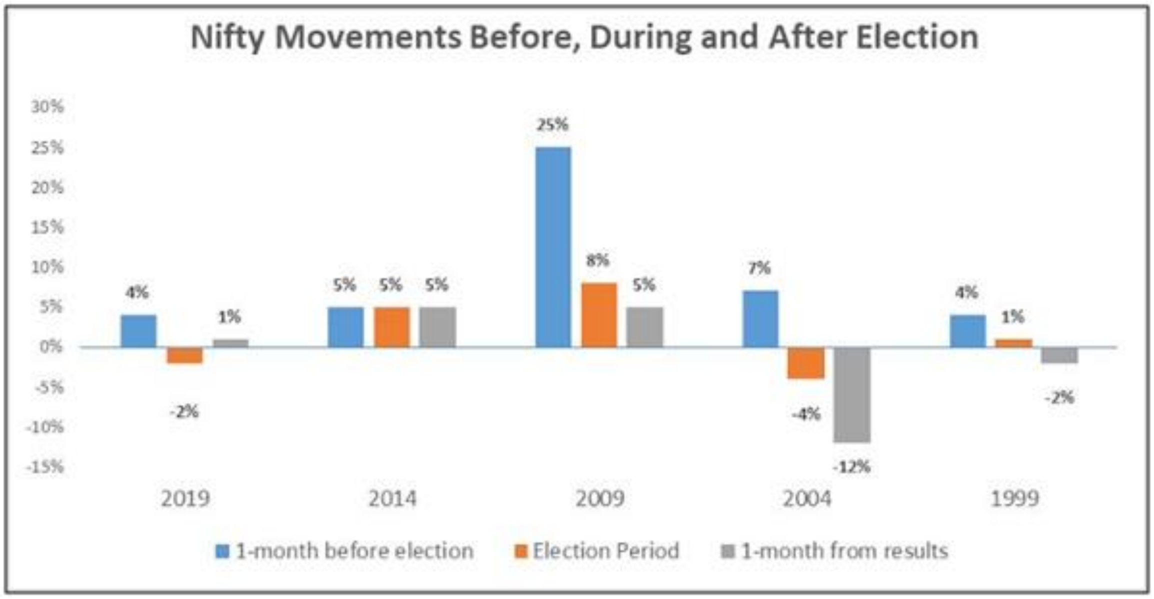
elections introduce volatility due to sporadic investor behaviour in the short term, the long-term effects are only really affected by the market-defining economic reforms and policies implemented by the ruling party. The **naturally volatile nature of the Stock Market is historically amplified** in the **direct aftermath of the elections**.



ELECTIONS & SENSEX

YEAR	INCUMBENT	NEWLY ELECTED	RESULTS DATE	SENSEX RALLY SIX MONTH TO ELECTIONS
1980	JP	INC	1/8/1980	0.5%
1984	INC	INC	12/21/1984	12.5%
1989	INC	Janata Dal	12/4/1989	0.1%
1991	Janata Dal	INC	5/27/1991	2.6%
1996	INC	United Front	5/23/1996	25.1%
1998	United Front	BJP	3/6/1998	-9.3%
1999	BJP	BJP	10/6/1999	31.6%
2004	BJP	INC	5/13/2004	9.1%
2009	INC	INC	5/18/2009	59.8%
2014	INC	BJP	5/16/2014	15.7%
2019	BJP	BJP	5/23/2019	9.8%

BJP= Bharatiya Janata Party, INC= Indian National Congress, JP= Janata Party
Source: SAMCO Securities

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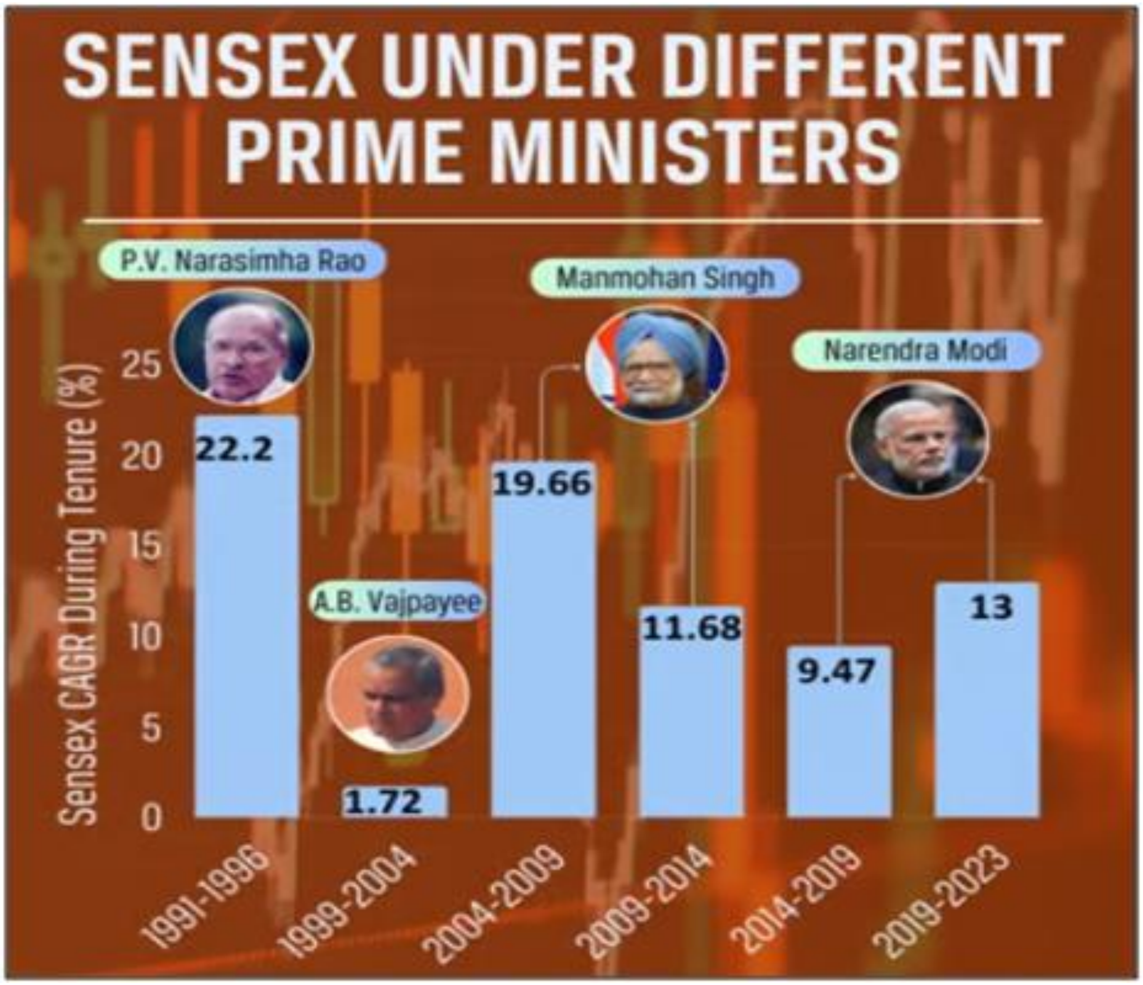
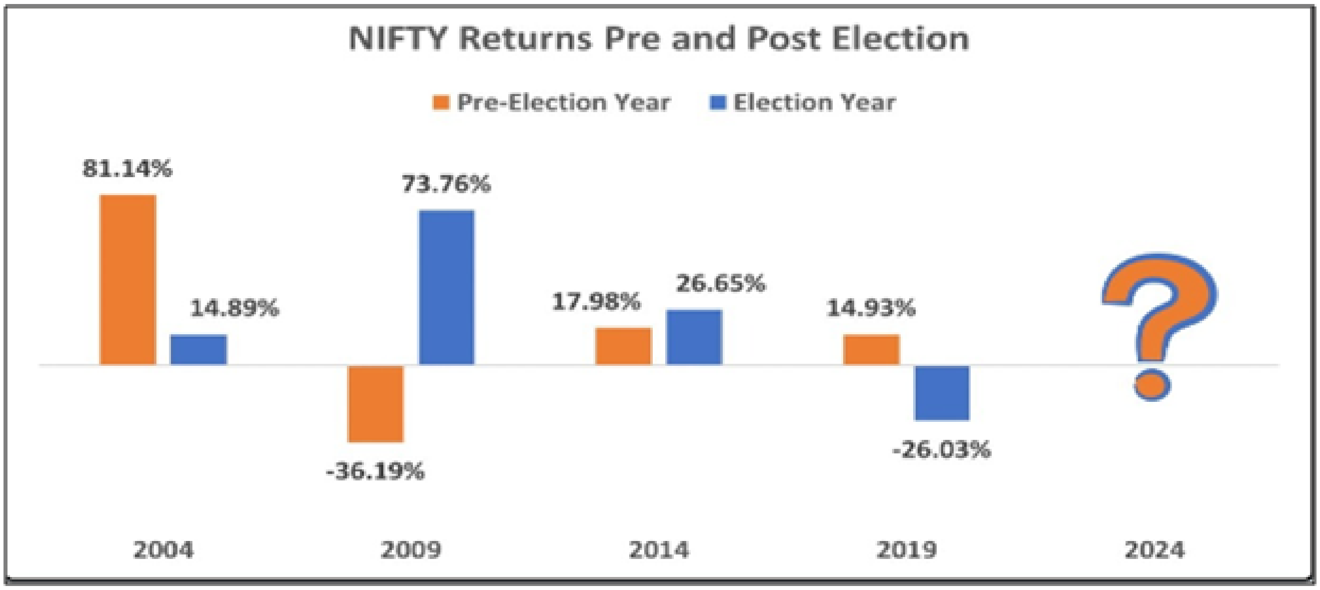
The stock market gets influenced by the Government's decisions on economy, trade practices, taxation, business laws, etc. Other factors that affect market performance are the availability of other investment assets, change in the composition of investors, and market sentiments.

HOW THE ELECTION RESULT HAVE AFFECTED SENSEX



Emotions play a crucial role in today's investment arena, for example as seen in the 2014 elections; investors were excited with the expectations that BJP will form the government and the market reflected a bullish run. Factors such as optimism, pessimism, confidence and irrational expectations, etc. are assumed to expound the dramatic upheaval of the progress of trading volumes and that of the returns. It has become a natural phenomenon to see the market behaving more volatile than usual when election results are announced. It is through the lens of behavioural finance that researchers have found the anomaly taking place at the time of the election.

HOW THE ELECTION RESULTS HAVE AFFECTED NIFTY OVER THE YEARS



This article focuses on analysing the impact of election result announcement on the performance of **Indian stock indexes Sensex (BSE) and Nifty (NSE)**. Many studies previously done have discussed the election effect on the stock market. This paper focuses on the election result effect on the stock market indexes of both the major exchanges in India.

Scholar's Opinions with respect to Impact of Elections on the Stock Market With Respect to Indian Markets

Campello (2007)– a Professor of Finance at the prestigious Cornell University and a renowned economist, through his study, highlight show general elections breed unease which may affect investors' decisions and psyche, which can, on a large scale- cause abnormality and bring about irregularities in the market. The Existence of Political risk is a ubiquitous phenomenon that has affected not just one, but many National Stock markets all across the world. The core reason behind the stock markets' inefficiency and volatility during these time periods may be attributed to political and economic unease that spawn unsound reactions. Many more studies reinforce the fact that the General election carries a significant impact on the behaviour of the market and thereby its correlating index movement.

Other Countries

Pedro and Valcanov (2003)- This paper analysed the nature of relationship observed between presidential elections and the stock market of the United States of America by sampling 684 monthly observations that included 18 elections within which 10 democratic and 8 Republican

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presidents were elected. Their study was based on data collected from 1927 onwards. The research established that **volatility is present in the stock market around election periods** with high sensitivity surrounding the result dates. Further through their research, they highlighted that the stock market returns were noticeably higher under Democratic presidencies as compared to Republican Presidencies. However, they were unable to explain this variation in returns, which still remains an unanswered mystery.

Aggarwal et al. (1999) –This study delved into the various kinds of events that correlate to massive shifts in the instability of emerging stock markets. The paper found **that most of these contingent events tend to stay local** and not international. The 1987 stock market crash was the only global event that may have been said to cause a significant increase in the volatility of several emerging markets.

Khalid et al. (2010)- This paper utilized the Markov Switching Process in studying the impact of Political Events on Financial Market Volatility. Taking an investigative approach towards the political shocks of the past, both negative and positive, this study managed to compile and study the data from Pakistan for the period ranging from January 1999 to September 2006. The research concludes by finding that different political events have undeniably caused setbacks and impacted the local economy severely.

Analysing the Data- In Brief

The patterns observed may indicate a relation more nuanced than what was before thought, which leads us to ponder the question; just how much influence does a ruling party command on the future of India's market?

Fluctuation in the stock market is generally based on the news which is related to economy, political events, weather conditions and foreign affairs. The objective of this study is to empirically analyse the effect of general elections on both NSE and BSE returns in pre-elections and post elections period and compare the variance of daily returns in the stock market for short term (10 days), medium term (20 days) & long term (30 days) in the direct aftermath of the pre-election and post- election period, aiming to highlight the impact of elections in creating a volatile market, at least in the short term.

For this analysis 5 election sessions were considered that ranges from 1998 – 2019. The daily closing prices of NIFTY & SENSEX index have been collected for a period from 1998 to 2019 which includes a total of 5 Lok Sabha elections. The time period of the study has been broadly divided into pre and post elections period.

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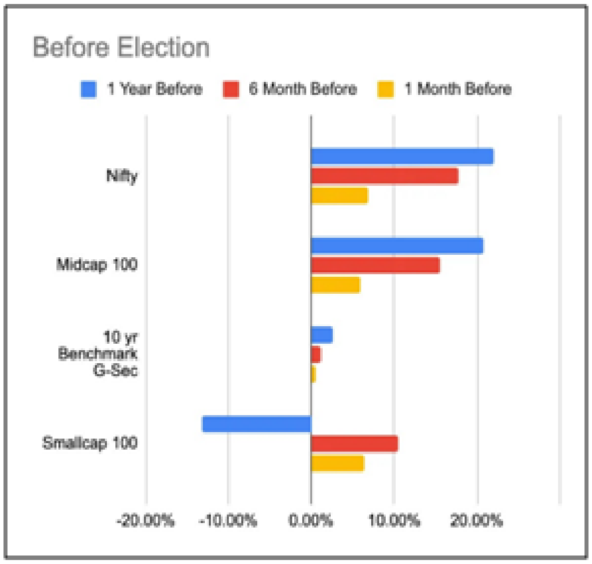

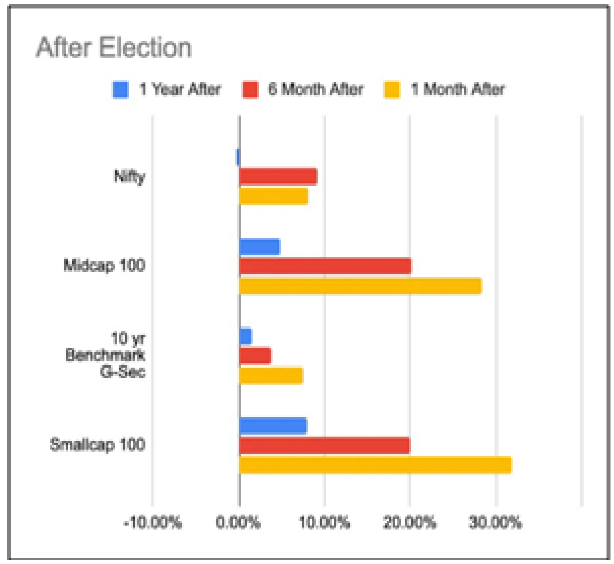

The Pre-Election period usually shows more movement than post as seen in the above pictures which are from the 2019 Lok Sabha elections.

6 months before Lok Sabha Election	Sensex Values	18 months post Lok Sabha Elections	Sensex Values	Returns Absolute (%)
30-May-89	692	27-May-91	1324	91%
17-Dec-90	1188	13-Dec-92	1860	57%
02-Dec-95	3035	28-Nov-97	3618	19%
27-Aug-97	4085	24-Aug-99	4792	17%
09-Apr-99	3423	05-Apr-01	3676	7%
12-Nov-03	4998	08-Nov-05	8353	67%
14-Nov-08	9267	11-Nov-10	20937	126%
13-Nov-13	20194	10-Nov-15	25743	27%

Analysing the Data- Statistically

Objectives of the Study

The objectives of the study also encompass the following:

- To analyse the impact of the general elections on both the NSE and BSE performance in pre-elections and post- elections period.

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- To analyse, compare and contrast the variance within daily returns of the stock market for short term (10 days), medium term (20 days) & long term (30 days) in the pre-elections and post- elections period.

Hypothesis

The following hypotheses has been framed:

H1: There is no significant impact of the general elections on both NSE and BSE returns.

Tools which help us with the analysis

T-Test- The 'T-Test' refers to a statistical examination of two population means. A double-sample t-test aims to check whether two samples are different in nature used when the variances of two normal distributions are unidentified and an experiment utilizes a small sample size.

METHODOLOGY

The daily closing prices of the NIFTY and SENSEX indexes have been compiled from the Yahoo finance website ranging from 1998 to 2014 which encompasses 5 Lok Sabha. The time period of the study may be broadly divided into the preand post elections period. 60 trading days' data surrounding the Lok Sabha elections period has been analysed. The time periods analysed in this paper may be classified into short term (10 days), medium term (20 days), long term (30 days) before and after the declaration of the Lok Sabha elections.

Tabular Representation of Data

Daily Average Return in Nifty Index							
Year	**Election Dates**	**X3**	**X2**	**X1**	**Y1**	**Y2**	**Y3**
		Last 30 Days	**Last 20 Days**	**Last 10 Days**	**Next 10 Days**	**Next 20 Days**	**Next 30 days**
1998	February-March	0.023	0.022	0.013	0.036	0.026	0.026
1999	September-October	0.017	0.016	0.013	0.047	0.05	0.049
2004	April-May	0.018	0.023	0.015	0.345	0.187	0.136
2009	April-May	0.048	0.035	0.024	0.341	0.82	0.137
2014	May	0.004	0.005	0.003	0.008	0.007	0.007

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Daily Average Returns in Sensex Index							
Year	**Election Dates**	**X3**	**X2**	**X1**	**Y1**	**Y2**	**Y3**
		Last 30 Days	**Last 20 Days**	**Last 10 Days**	**Next 10 Days**	**Next 20 Days**	**Next 30 days**
1998	February-March	0.02	0.02	0.02	0.03	0.03	0.02
1999	September-October	0.02	0.01	0.02	0.01	0.03	0.04
2004	April-May	0.02	0.02	0.02	0.26	0.14	0.1
2009	April-May	0.06	0.04	0.02	0.34	0.17	0.13
2014	May	0.005	0.004	0.005	0.009	0.007	0.007

Shows Paired t-test for Nifty Index						
	X3 & Z	**X2 & Z**	**X1 & Z**	**Y1 & Z**	**Y2 & Z**	**Y3 & Z**
Actual	-1.213396	-1.216333	-1.228762	-0.949026	-1.081857755	-1.122480837
Table Value (5%)	2.78	2.78	2.78	2.78	2.78	2.78

Shows Paired t-test for Sensex Index						
	X3 & Z	**X2 & Z**	**X1 & Z**	**Y1 & Z**	**Y2 & Z**	**Y3 & Z**
Actual	0.31780871	0.0272538	-0.641754651	0.582771517	1.003644083	1.237447649
Table Value (5%)	2.78	2.78	2.78	2.78	2.78	2.78

Impact of Election on Nifty									
	SHORT TERM PERIOD			**MEDIUM TERM PERIOD**			**LONG TERM PERIOD**		
	X3 & Y1	**X2 & Y1**	**X1 & Y1**	**X3 & Y2**	**X2 & Y2**	**X1 & Y2**	**X3 & Y3**	**X2 & Y3**	**X1 & Y3**
Actual	-1.84210220	-1.84763256	-1.90715817	-1.96509539	-1.98393760	-2.10546124	-2.10066460	-2.1298	-2.3036
Table Value (5%)	2.78	2.78	2.78	2.78	2.78	2.78	2.78	2.78	2.78

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Impact of Election on Sensex									
	SHORT TERM PERIOD			MEDIUM TERM PERIOD			LONG TERM PERIOD		
	X3 & Y1	X2 & Y1	X1 & Y1	X3 & Y2	X2 & Y2	X1 & Y2	X3 & Y3	X2 & Y3	X1 & Y3
Actual	-0.670	-0.621	-1.261	-0.807	-0.788	-1.154	-0.854	-0.892	-1.151
Table Value (5%)	2.78	2.78	2.78	2.78	2.78	2.78	2.78	2.78	2.78

Inference Drawn from Data

10 Days

The observed result of the paired sample through t-test proved to be noticeable, indicating that there is, in fact a **slight increase in the returns** from the pre- to post-election period of time. The research disproves the hypothesis H1 there is a significant impact of the General Elections on the returns in the very short-term period of CNX Nifty and Sensex.

20 Days

A paired sample t-test was conducted in order to ascertain whether a statistically significant variance existed between the returns of the 20 days pre- and post-election period. The result of the sample test proved to not be significant, indicating that there is an increase in the returns from the pre-Election period to the post-Election period. The research sustains the hypothesis within this specific time period as there is **no significant impact of Election on the returns of medium-term period.**

30 Days

A paired sample t-test was conducted in order to ascertain whether a statistically significant variance existed between the returns of the 30 days pre- and post-election period. The result of the sample test proved to not be significant, indicating that there is a significant increase in the returns from the pre-Election period to the post-Election period. The research sustains the hypothesis within this specific time period as there is no significant impact of Election on the returns of medium-term period. Therefore, **there is no impact of Election the returns of long-term period in CNX Nifty and Sensex.**

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Conclusion

The article concludes by reiterating Hypothesis 1 that the General Election **result does not result in a noteworthy effect on the stock market**. Although, it does **foster a very volatile nature in the market** in the immediate lead up to the elections and the immediate period succeeding the announcements of the results as depicted by daily average returns.

On the sociological aspect of things, the empirical data indicates that investors tend to ride on the policies, ideology and political will of the party in contention (and the party in power soon after the election) resulting in them betting on the bull and bringing the bears down.

The statistics also indicate that the stock market is **more affected in the pre-election period as compared to the post-election timeframe.** The stock market may be influenced by the Government's decisions on economy, trade practices, taxation, business laws, etc. that may be pre-empted by investors. Effectively, the investors in investing in certain companies also bet on the winner of the election. The **emotion of the market and nature of humans also clearly affects the market.**

For instance, in the 2014 elections; investors were excited with the expectations that the BJP party would form the government and the market thereby reflected a bullish run. Factors such as optimism, pessimism, confidence and irrational expectations, etc. are assumed to expound the dramatic upheaval of the progress of trading volumes and that of the returns. It has become a natural phenomenon to see the market behaving abnormally when election results are announced.

On the practical side of things, it must be noted that one can also benefit with the application of short-term market strategy during this period of volatility, given the smart application of calculated risks. More events like the Union Budget, elections, festivals, mergers and acquisition, share splits, bonus announcement, wars, etc., always results in a slight market shift. Specific stock market sectors and key policy issues are to be observed with a watchful eye in election years While the analysis does not point towards elections carrying a meaningful medium-to-long-term market effect, they may affect individual sectors and industries more harshly than they do others, which offers scope for further research. Different election outcomes have the propensity to affect proposed policies, regulations, or global conflicts.

The following are some policy issues that may be used to monitor throughout election process:

- Spending priorities, such as Infrastructure and Defence
- Healthcare
- Regulation

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- Immigration policy
- Geopolitical conflicts

The study aims to aid investors in understanding the necessity to invest cautiously and may offer guidance on making wise investment decisions around the timeframe of the general. This study will help investors minimize their overall risk and maximize returns of their investments.

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