THE EFFECTS OF INTEREST RATE CHANGES
ON
STOCK PRICES OF BANKS IN CHINA

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DECLARATION

I hereby declare that the project paper is based on my original work except for quotations and citations that have been duly acknowledge. I also declare it has not been previously or concurrently submitted for any other Master's programme at Universiti Utara Malaysia or other institutions.

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ABSTRACT

This paper presents the interest rate effects on the banking stock prices in China. It focuses on the announcement dates to measure the effects of interest rate changes on the bank stock returns. The study chooses four interest rate increases and four decreases during 2002-2010. The study finds that there is normally a negative relationship between interest rate changes and stock returns. When interest rate increases, stock prices decreases, and when the interest rate decreases, the stock prices increases in China.

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Chapter One

Introduction

1.1 Background

This paper is a study of what interest rates can do to the stock market especially banking stock prices. The study will pay special attention to China while looking at the phenomena elsewhere. It is an event study, looking at situations before, during and after interest rate changes. Market interest rates directly reflect the use of funds for credit relation, the cost to the debtor is the creditor's right for compensation. From the perspective of macroeconomic analysis, interest rate volatility reflects changes in the supply and demand situation of the market during different stages of economic development. Market performances are affected by different interest rates. When there is a capital shortage, there is a rise in the interest rates. When there is a market slump, during a recession, interest rates decrease with a reduction in the demand for capital. In the overall economy interest rates impact people's savings, investments and consumer behaviors. Interest rate structures also affect the structure of the securities held. In theory, interest rates and stock prices are generally inversely proportional. When interest rates rise, stock prices fall and when interest rates decline, stock prices rise.

This is because, first of all, interest rates lead to an adjustment to the cost of funds of listed companies, affecting the profitability of listed companies. When the central bank raises lending rates, the rise in the interest burden falls on the business by

The contents of the thesis is for internal user only

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