

Impact of Macroeconomic Factors on Stock Prices: Empirical Evidence from the Colombo Stock Exchange

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Abstract

Stock price volatility in emerging markets is strongly shaped by macroeconomic dynamics, yet Sri Lanka's specific context remains underexplored. While previous studies have largely focused on developed and major emerging economies, there is a clear research gap regarding how Sri Lanka's economic conditions influence equity markets. This study bridges that gap by analysing the impact of gross domestic product (GDP) growth, inflation rate, interest rate, and exchange rate on stock price performance in the Colombo Stock Exchange (CSE), measured by the All-Share Price Index. The theoretical foundation is based on the Efficient Market Hypothesis and Arbitrage Pricing Theory, which explain how macroeconomic variables affect stock market behaviour. Monthly secondary data from January 2014 to December 2024 were obtained from the Central Bank of Sri Lanka and the CSE. The population comprises all listed companies on the CSE, represented by the ASPI as the market index, so separate sampling was not required. Analytical techniques include descriptive statistics, Pearson correlation analysis, and multiple linear regression, performed using EViews software to ensure robust statistical testing. The results reveal that GDP growth positively influences the ASPI, while the interest rate exerts a significant negative effect. In contrast, inflation and exchange rate fluctuations show no statistically significant relationship with stock prices. These findings highlight the critical role of economic growth and monetary policy in shaping Sri Lanka's equity market trends. Beyond providing practical insights for investors and policymakers, this study enriches the limited South Asian literature on emerging markets by offering country-specific evidence, expanding theoretical understanding of macroeconomic-stock price linkages in smaller developing economies, and informing future research on emerging market dynamics in South Asia.

Keywords: Colombo Stock Exchange, emerging markets, macroeconomic variables, Sri Lanka, stock prices