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Nexus Between Sectoral Shift and Stock Return:
Insights From Bangladesh

Mosharrof Hosen, Faculty of Business and Finance, Universiti Tunku Abdul Rahman, Kampar, Malaysia
https://orcid.org/0000-0002-9301-4318

Mohammed Imran, DualConcept, Jakarta, Indonesia
https://orcid.org/0000-0003-1011-4258

Mohammad Ashraful Ferdous Chowdhury, Department of Business Administration, Shahjalal University of Science and Technology, Bangladesh
https://orcid.org/0000-0001-8540-1353

ABSTRACT

The objective of this study is to examine the impact of sectoral shift on the stock return of Bangladesh. This study employs auto-regressive distributive lag (ARDL) approach using the weekly data of various sectoral indices of Bangladesh over the period from May 1999 to September 2016. The findings tend to indicate that there has possible sectoral portfolio diversification in the market and 'general product industry' is the most exogenous and profitable sector from the rest. This study is one of the first attempts of the sectoral analysis and its impact on the stock return with the reference to Bangladesh. Furthermore, this study can be a benchmark for the policymakers of emerging economies to find the impact of economic transformation in the stock returns of the equity markets.

KEYWORDS

ARDL, General Industry, Sectoral Diversification, Stock Return

1. INTRODUCTION

The sectorial investigation is employed by financial analysts who are to choose better stocks to put their resources into it. The financial analysts distinguish most encouraging segments and evaluate the performance of respective companies within the sector to figure out which remarkable stock would give better returns and at last, be purchased (Abuzayed, Al-Fayoumi, & Molyneux, 2018). Markowitz (1952 and 1959) explored that sectoral diversification can help investors by decreasing volatility as well as afterward, investment jeopardy which is also supported by many studies and researchers. Moreover, nowadays a sectoral diversified investment approach is commonly used by numerous universally successful stockholders (Barbieri & Consoli, 2019; Maheshwari, Gupta, & Li, 2018).

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The performance of a company's stock in the capital market is generally affected by two significant aspects which are first, the individual company's performance and second aspect mainly consider the overall performance of the whole sector where the respective company belongs (Bebczuk & Galindo, 2008). As investors know that a similar function in the economy is performed by the sectors which consist of a group of companies. However, the sectoral analysis can be done by dividing the total market into the sector and after that justifying the performance of each sector which will also lead to know the comparison feedback between each sector or whole market (Chowdhury, Bhattacharya, Mallick, & Ulubaşoğlu, 2014).

According to Mohamad, Hassan, and Sori (2006), a sectoral diversified investment portfolio can be attained in different ways such as through investing in diverse intercontinental markets, numerous asset classes and/or crosswise various industries or sectors. In similar kind of study, Grubel (1968) found that the most optimum amount of benefits can earn from global diversification of investment in respect to best fit by using finance to discover the finest conceivable amalgamation of markets around the world. Economic industries and sectors, thus, also allow us to do the diversification because of the potential changes in performances within each economic cycle or market circumstances. Due to that, a specific sector or a company cannot always be the highest or worst performer all the time (Grillitsch & Asheim, 2018).

The comovement and correlation between the stocks are the crucial maiden elements for the diversification. The gain can earn from a portfolio with stocks, therefore, when there has an adverse or little correlation among themselves that leads to reducing risk. Several researchers have demonstrated that the nature of correlation may not be stable for a particular period (Preis, Kenett, Stanley, Helbing, & Ben-Jacob, 2012). The actual risk may be varied due to the time fluctuating feature of the stock market which leads to getting diverse risk at a different time in the portfolio. However, many researchers have focused on this issue, correlation, and comovement of the stock market, in a different way including crisis period facing by all over the world (Rastogi, 2014).

Some studies also have concentrated, more precisely, on a different feature of correlation such as the correlation between markets (Gupta & Donleavy, 2009; Syllignakis & Kouretas, 2011). Some investors are more concerned to get long-term gains, but some stakeholders are only interested in getting short-term profits from the investment. Moreover, short-term correlation and fluctuation were expected in the former, but though nowadays the stakeholders are more interested in the short-term fluctuation and comovements (Masood, Bellalah, Chaudhary, Mansour, & Teulon, 2010).

The connection between macroeconomic factors and stock market returns is, at this point, very much archived in the literature (Singh, Mehta, & Varsha, 2011; Flannery & Protopapadakis, 2002). Nevertheless, almost no writing identifies with looking at the cointegration between sectorial shift and stock markets' indices. Therefore, country impacts have been an overwhelming part of clarifying varieties in stock returns, even in the developed markets, and investors have segmented their allocations accordingly. This study set out to investigate whether sectoral portfolio opportunities still prevails in Bangladesh economy or not. So, the main objective of the study is to find the sector-wise portfolio opportunity in Bangladesh by using ARDL bounds testing approach. This study effort to examine the probable investment diversification strategies based on various economic segments for the case of Bangladesh. The maiden question needs to answer is whether there are any potentialities for investors in Bangladesh to classify and expand their investment across segments and markets.

Most of the previous studies were inconclusive because they examined that the intercontinental stock market comovement in respect of returns and volatility. Hence, the majority percent of those studies have been done based on grouped market indices or between diverse countries around the world (Gupta & Basu, 2011). The current authors claim that, for instance, some empirical researches have made a comparison by including their new data of stock markets comovements in the established economies in contradiction of the emerging markets, or among regions, with the Middle East, the Asia Pacific, Euro area and North Africa (MENA) (Balli & Balli, 2011; Rua & Nunes, 2009; Vo, Pham, Pham, Truong, & Nguyen, 2018). The current study analysis this issue only for a single country

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