

The Effect of Economic Factors on Saudi Share Index

Hamad AL-Towaijri*

Abstract

This paper aims to examine the major economic factors which affect the Saudi stock market. The model, which is used in this paper, includes major macroeconomic variables which are expected to affect the stock market. These variables are the real gross domestic product, oil prices, money supply (M1), inflation rate, and interest rate. The paper use co-integration tests and error correction model to examine the economic factors that affect the stock market in the short and long runs terms.

Using quarterly data from 1985:1 to 2007:4. Estimation results indicate the importance of economic factors in explaining the fluctuations in Saudi share index in the long run, the gross domestic product, the oil prices, the money supply are positively related to the stock market index, while the inflation and the interest rate are negatively correlated to the stock market index, However, the effect of economic variables on the stock market index is weak in the short run which suggests that the sociological factors and speculations which are introduced to the model to explain the short run fluctuation in the stock market especially after the sharp decrease and the hard collapse in the share index, in the first quarter of 2006.

* Hamad AL-Towaijri
Economics Department , King Saud University
hamad_towaijri@yahoo.com