ABSTRACT

This paper aims to empirically examine the causal relationship between BSE stock returns and the foreign exchange markets of seven of India's major trading partners in terms of trade volume. The methodology used is pairwise Granger Causality test. The data taken is for the exchange rates of India with China, South Korea, Indonesia, Malaysia, Hong Kong, United States and Germany from 2001 to 2015. We also attempt to explain the asset market contagion through the 2008 global meltdown. The correlation between returns and exchange rates comes out to be slightly negative and Granger causality is proven for each of the markets**.**

The results of this study indicate a presence of at least unidirectional causality of Indian stock markets with each of the seven currency markets. Structural break in results is also seen by splitting the data into two before and after the 2008 global meltdown, suggesting presence of contagion.

Keywords : Stock returns, exchange rates, volatility spillovers, Granger causality, market contagion.