

Stock Returns in the USA and the Effect of Macroeconomic Variable Uncertainty

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Abstract

Stock market returns have long been a subject of interest for investors and economists alike. The United States has one of the most developed and dynamic stock markets in the world and its movements can have far-reaching effects on the global economy. While many factors can influence stock market returns, one significant factor that has received increased attention in recent years is macroeconomic variable uncertainty. Macroeconomic variable uncertainty refers to the degree of unpredictability or ambiguity surrounding key economic indicators such as inflation, interest rates, and GDP growth. When these variables are uncertain, investors may be less willing to take risks, which can lead to increased volatility in stock prices. Uncertainty can arise from a variety of sources, including changes in government policies, geopolitical events, and fluctuations in commodity prices.

Keywords: Risk factors • Stock returns • Uncertainty

Introduction

Numerous studies have investigated the relationship between macroeconomic variable uncertainty and stock returns in the United States. One notable finding is that uncertainty tends to have a negative impact on stock prices. For example, a study by Baker, Bloom, and Davis (2016) found that increases in macroeconomic policy uncertainty were associated with significant declines in stock prices. However, the relationship between uncertainty and stock returns is not always straightforward. In some cases, uncertainty may actually increase stock prices if investors believe that the uncertainty will lead to future profits.

Literature Review

A new technological breakthrough may lead investors to invest in companies that are likely to benefit from the development, driving up their stock prices. One factor that can influence the impact of uncertainty on stock returns is the nature of the uncertainty itself. Some types of uncertainty may be more damaging to stock prices than others. For example, uncertainty surrounding government policies may be more damaging than uncertainty surrounding technological innovations. This is because government policies have a greater potential to disrupt the economy and corporate earnings. Another factor that can influence the impact of uncertainty on stock returns is the degree of investor risk aversion. When investors are more risk-averse, they may be more likely to sell their stocks in response to uncertainty, leading to lower stock prices. Conversely, when investors are less risk-averse, they may be more willing to hold onto their stocks in the face of uncertainty, which could lead to higher stock prices. The impact of uncertainty on stock returns may also depend on the timing of the uncertainty. For example, uncertainty that arises during periods of economic expansion may have a different impact on stock prices than uncertainty that arises during periods of economic contraction.

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Discussion

It has been extensively researched how macroeconomic factors and stock returns relate. State variables that characterise the economy are defined by Chen et al. (1986), who also look into how they affect asset prices. Future cash flows are discounted using the appropriate discount rate to arrive at asset valuations. When they looked at the state variables that affect these two variables, they discovered that industrial production, shifts in risk premiums, and twists in the yield curve were important drivers in determining asset values. Contrarily, consumption and oil prices were shown to be negligible state factors, and changes in predicted inflation only partially influenced asset values. A research on the impact of macroeconomic factors on stock prices for 10 European nations was undertaken by Asper in 1989. Employment, imports, inflation, and interest rates have all been demonstrated [1-3].

Measuring the impact of macroeconomic factors on stock prices for 10 different European nations. It has been demonstrated that changes in stock values are adversely correlated with employment, imports, inflation, and interest rates, but favourably correlated with future real activity, measures of money, and the U.S. yield curve. According to Gjerde and Sættem (1999), changes in the real interest rate and the price of oil have a major influence on Norwegian stock returns. Cheung and Ng (1998) found that the real oil price, real production, real money supply, and real consumption were important state factors in explaining national stock market indices using quarterly data from Canada, Germany, Italy, Japan, and the U.S.

Humpe and Macmillan (2009) discovered that, with a focus on the United States, stock prices were positively correlated with industrial production the consumer price index and the long-term interest rate were shown to be negatively correlated. The money supply and stock returns were shown to have a negligible connection. The relationship between stock prices and industrial production and the long-term interest rate are both confirmed by Ratanapakorn and Sharma (2007) to be positive and negative, respectively. The money supply, inflation, exchange rate, and the short-term interest rate are all said to have positive relationships with stock values [4-6].

Conclusion

In conclusion, macroeconomic variable uncertainty can have a significant impact on stock returns in the United States. While uncertainty may sometimes lead to higher stock prices, in many cases, it is associated with lower prices. The impact of uncertainty on stock prices depends on a variety of factors, including the nature of the uncertainty, investor risk aversion, and the timing of the uncertainty. Ultimately, investors should take a holistic approach to investment decision-making, considering a wide range of factors when making investment decisions.

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Conflict of Interest

There are no conflicts of interest by author.

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