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### Empirical Evidence on Nexus between Financial Markets in India: An ARDL Bounds Test Approach

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#### ABSTRACT

In the aftermath of global financial crisis, the study of the relationship between financial markets has become a moot point in the finance literature. In the literature, there is no much theoretical and empirical consensus on the interrelationship between the indicators of financial markets. Thus, it is imperative to conduct an empirical investigation of the causal relationship between financial markets in an emerging market economy like India. The application of ARDL bounds test provides the evidence of the existence of the long-run equilibrium relationship between the money and capital markets, and also between foreign exchange and money markets in India. However, no causal relationship runs from foreign exchange and capital markets to the money market in the long-run. This finding is very important in the context of inflation and interest rate structure in India.

**JEL Classification Code:** C32, E44, G19

**Keywords:** Financial Markets, Interest Rate, Foreign Exchange Rate, Stock Price Index, India.

#### 1. INTRODUCTION

In the aftermath of the global financial crisis, the study of relationship between financial markets has become a moot point in the finance literature. Indian financial sector has been witnessing an emerging trend due to the introduction of both domestic and external financial liberalizations since early 1990s. In the literature, it has been argued that financial liberalization enhances real economic growth through a developed financial system (Shaw, 1973). Financial liberalization also contributes to the process of integration of financial markets within and across countries. Domestic financial liberalization leads to the removal of the entry barriers and to the elimination of administered interest rates while external financial liberalization contributes to