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RESERVE BANK OF INDIA

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January 11, 2022

RBI Working Paper No. 01/2022: Stock Price Reaction on the Announcement of Basel Implementation: Evidence from Indian Banks

Today the Reserve Bank of India placed on its website a Working Paper titled "[Stock Price Reaction on the Announcement of Basel Implementation: Evidence from Indian Banks](#)" under the Reserve Bank of India Working Paper Series*. The paper is authored by Gaurav Seth, Supriya Katti and B.V. Phani.

The study evaluates the market reaction of different policy decisions taken by the Reserve Bank of India (RBI) to bring in major reforms in the Indian banking industry after the financial liberalisation to align its domestic regulations with global Basel capital adequacy norms. These announcements are some of the important decisions that have brought in critical changes in the operations of Indian commercial banks; therefore, it is imperative to understand how the market perceives the implementation of Basel recommendations. Event studies are used to examine the short-run effect of regulations. Using the same methodology, the study reveals that the Indian banks were initially not prepared to raise the capital to 9 per cent, which resulted in the market overreacting to the Basel I announcement, and pessimistic sentiments were observed in terms of abnormal returns and cumulative returns. The subsequent announcements received a positive reaction since Indian banks were benefitted from the experience gained by the imposition of previous regulatory decisions and were prepared to cope with the expected changes. The rise in stock prices of banks during the announcements of Basel II and Basel III periods provides the evidence that implementation of the Basel regulations has a favourable impact on the Indian banking sector in the long run. The response of the market also varied depending upon ownership structure and policy decisions for public sector banks and private sector banks. Further, the multivariate analysis does not show any significant impact of bank-specific characteristics on the market performance of various events. This study contributes to the growing literature on the wealth effect of the implementation of Basel risk-based capital adequacy norms on differentiated bank ownership structure in the emerging markets.

Press Release: 2021-2022/1528

(Yogesh Dayal)
Chief General Manager

* The Reserve Bank of India (RBI) introduced the RBI Working Papers series in March 2011. These papers present research in progress of the staff members of the RBI and at times also those of external co-authors when the research is jointly undertaken. They are disseminated to elicit comments and further debate. The views expressed in these papers are those of the authors and not necessarily those of the institution(s) to which they belong. Comments and observations may please be forwarded to the authors. Citation and use of such papers should take into account its provisional character.