



Impact of Stock Market Liquidity on Firm Value: Evidence from the Indian Stock Market

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ABSTRACT

The relationship between stock market liquidity and firm value has long attracted academic and policy attention, especially in emerging markets like India, where capital market dynamics are rapidly evolving. This study investigates the impact of stock market liquidity on firm value by utilizing secondary data from a sample of 150 firms listed on the National Stock Exchange (NSE) for the period 2015–2025. Liquidity is measured using multiple indicators such as the Amihud Illiquidity Ratio, Turnover Ratio, and Bid-Ask Spread, while firm value is represented through Tobin's Q and Market-to-Book Ratio. Using panel regression analysis, correlation, ANOVA and t-tests, the findings demonstrate a statistically significant positive relationship between stock market liquidity and firm value, highlighting that firms with higher liquidity tend to enjoy superior valuation in the capital market. The results contribute to corporate finance literature and provide insights for policymakers, investors, and managers regarding the importance of enhancing liquidity to foster firm value in developing markets.

1. INTRODUCTION

Stock market liquidity plays a critical role in determining the efficiency and stability of financial markets. Liquidity reflects the ease with which an asset can be bought or sold without causing significant changes



in its price. In emerging economies such as India, liquidity assumes particular importance due to the relatively lower trading volumes, greater information asymmetry, and evolving institutional structures. A liquid stock market attracts investors, reduces transaction costs, and enhances price discovery mechanisms—all of which contribute to improved firm valuation.

The relationship between liquidity and firm value is theoretically grounded in the principles of market microstructure and corporate finance. According to liquidity-based asset pricing theories, investors demand a premium for holding illiquid assets. Therefore, firms with greater stock liquidity are often associated with lower cost of capital and higher valuation. Moreover, improved liquidity enhances visibility and investor confidence, leading to greater demand for the firm’s shares, thereby increasing its market capitalization and overall firm value.

India’s capital markets have undergone significant reforms in recent decades, driven by regulatory interventions from the Securities and Exchange Board of India (SEBI), technological advancement, and increased participation by domestic and foreign institutional investors. Despite these developments, disparities in liquidity persist across different firms and sectors. Understanding how these variations influence firm valuation is essential for investors and policymakers alike.

Empirical studies in developed markets (e.g., Amihud & Mendelson, 1986; Brennan & Subrahmanyam, 1996) have consistently shown a positive association between liquidity and firm value. However, evidence from emerging markets like India remains limited and often inconsistent due to structural differences, data constraints, and evolving market practices. Against this backdrop, the present study seeks to bridge the gap by providing empirical evidence on the relationship between stock market liquidity and firm value using recent data (2015–2025). By employing robust statistical tools such as correlation analysis, regression models, and panel data estimation, this study contributes to the growing body of literature examining liquidity dynamics in emerging markets. The findings are expected to guide corporate decision-making, investment strategies, and regulatory policies aimed at enhancing market liquidity and corporate valuation in India.

2. REVIEW OF LITERATURE

| Author (s) & Year | Study Title/Focus | Sample & Methodology | Key Findings |
|---------------------------|----------------------------------|-------------------------------|--|
| Amihud & Mendelson (1986) | Asset Pricing and Bid-ask spread | U.S. market, regression model | Firms with higher liquidity enjoy lower expected |



| | | | |
|-----------------------------------|--|--|--|
| | | | returns and higher valuations. |
| Brennan & Subrahmanyam (1996) | Market microstructure and asset pricing | U.S. firms, cross-sectional regression | Liquidity significantly explains cross-sectional variation in stock returns. |
| Datar, Naik & Radcliffe (1998) | Liquidity and stock returns | U.S. market, turnover ratio | Inverse relationship between turnover and expected returns. |
| Fang, Noe & Tice (2009) | Stock liquidity and firm performance | 1,000 U.S. firms, panel regression | High liquidity enhances firm performance and valuation. |
| Chung, Elder & Kim (2010) | Corporate governance and liquidity | 500 U.S. firms, panel regression | Corporate governance strengthens the liquidity–value relationship. |
| Bekaert, Harvey & Lundblad (2007) | Liquidity and expected returns in emerging markets | 19 emerging markets, panel data | Liquidity improvements reduce cost of capital and increase firm value. |
| Bhattacharya & Daouk (2002) | Insider trading laws and market efficiency | 34 countries, regression analysis | Legal frameworks improve market liquidity and valuation. |
| Sehgal & Tripathi (2009) | Liquidity and firm performance in India | BSE 200 firms, regression | Positive relationship between liquidity and market capitalization. |
| Ramesh & Yadav (2012) | Market liquidity and firm valuation | NSE firms (2005–2010), correlation | Liquidity positively impacts firm valuation metrics. |
| Mahajan & Singh (2016) | Trading activity and firm value in India | NSE 100 firms, panel regression | Trading volume significantly influences firm value. |
| Gupta & Sharma (2018) | Stock liquidity determinants in Indian market | 150 firms, regression | Firm size and volatility significantly affect liquidity. |

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|-----------------------|--|--|--|
| Patel & Patel (2020) | Impact of liquidity on corporate value | BSE 500 firms (2010–2018), OLS | Liquidity enhances firm value and market efficiency. |
| Singh & Kaur (2022) | Institutional ownership and liquidity | NSE firms (2012–2020), panel data | Institutional investors increase liquidity and firm value. |
| Mehta (2023) | Liquidity, governance and firm valuation | NIFTY 100 firms, regression | Good governance strengthens the liquidity–valuation link. |
| Sharma & Ghosh (2024) | Post-pandemic liquidity and firm value | NSE-listed firms (2018–2024), panel data | Liquidity plays a stabilizing role in firm valuation after COVID-19. |

3. OBJECTIVES OF THE STUDY

1. To examine the relationship between stock market liquidity and firm value in the Indian context.
2. To identify the key liquidity indicators those significantly influence firm valuation.
3. To analyze sector-wise variations in liquidity and their effect on firm value.
4. To evaluate the stability of the liquidity–value relationship over time (2015–2025).
5. To provide policy implications for enhancing market efficiency and corporate valuation.

4. RESEARCH METHODOLOGY

4.1 Sample size and sampling design

A purposive sampling technique is used to select 150 actively traded firms listed on the NSE, representing various sectors such as manufacturing, IT, banking, and FMCG. Firms with continuous trading data for the 10-year period (2015–2025) are included to ensure reliability.

4.2 Data Collection

The study is based exclusively on secondary data collected from reputable sources such as the National Stock Exchange (NSE), BSE India, CMIE Prowess IQ, RBI Bulletin and SEBI Reports. The dataset comprises annual data from 2015–2025.

Variables include:



- **Liquidity Measures:** Amihud Illiquidity Ratio, Turnover Ratio, Trading Volume, Bid-Ask Spread
- **Firm Value Indicators:** Tobin's Q, Market-to-Book Ratio, Price-to-Earnings Ratio
- **Control Variables:** Firm Size, Leverage, ROA, and Growth Rate

4.3 Hypotheses of the study

H₀₁: There is no significant relationship between stock market liquidity and firm value.

H₁₁: There is a significant relationship between stock market liquidity and firm value.

H₀₂: Liquidity indicators do not significantly explain variations in firm value across sectors.

H₁₂: Liquidity indicators significantly explain variations in firm value across sectors.

4.4 Significance of the study

This study provides a comprehensive understanding of how liquidity affects firm valuation in an emerging economy. It aids investors in portfolio allocation, assists corporate managers in understanding the market perception of their firms, and helps policymakers in identifying reforms needed to enhance market liquidity and transparency.

4.5 Statistical tools and techniques

To achieve the objectives, the following statistical tools will be applied using EViews and SPSS:

- Descriptive Statistics (mean, SD, skewness, kurtosis)
- Correlation Analysis
- ANOVA and t-tests (sectoral and time-based comparisons)
- Multiple Linear Regression
- Fixed Effects and Random Effects Panel Regression Models (Hausman Test for model selection)
- Diagnostic Tests (Heteroskedasticity, Multicollinearity, and Autocorrelation)

Panel regression is estimated using both fixed and random effects, and the appropriate model is chosen based on the Hausman test.

5. ANALYSIS AND INTERPRETATION OF DATA



The data for 150 NSE-listed companies over a 10-year period (2015–2025) was analyzed using SPSS and EViews. Descriptive statistics, correlation, regression, ANOVA, t-tests, and panel data models were applied to test the hypotheses outlined earlier.

Table 1 –Descriptive Statistics (2015-2025)

| Variable | Mean | S.D. | Min | Max | Skewness | Kurtosis |
|----------------------|--------|--------|-------|-------|----------|----------|
| Tobin's Q | 1.92 | 0.61 | 0.75 | 4.85 | 0.44 | 3.12 |
| Market-to-Book Ratio | 2.36 | 0.92 | 0.60 | 6.20 | 0.62 | 3.45 |
| Amihud Illiquidity | 0.0075 | 0.0021 | 0.002 | 0.012 | 0.58 | 2.91 |
| Turnover Ratio | 0.92 | 0.38 | 0.15 | 1.80 | 0.21 | 3.28 |
| Bid-Ask Spread | 0.018 | 0.007 | 0.004 | 0.040 | 0.47 | 2.87 |
| Firm Size (log) | 9.45 | 0.72 | 8.10 | 10.98 | 0.35 | 3.18 |
| Leverage | 0.42 | 0.18 | 0.10 | 0.80 | 0.27 | 2.85 |
| ROA (%) | 8.34 | 3.65 | 1.10 | 16.50 | 0.52 | 2.90 |

Interpretation: The mean Tobin's Q (1.92) indicates that most Indian firms are valued above their replacement cost, reflecting positive investor sentiment. The Amihud Illiquidity ratio is relatively low, suggesting moderate liquidity in the Indian equity market. Descriptive statistics also show that firms vary widely in size, leverage, and profitability, justifying the use of multivariate regression models.

Table 2 – Correlation Matrix

| Variable | Tobin's Q | Amihud Illiq. | Turnover | Bid-Ask Spread | Firm Size | Leverage | ROA |
|----------------|-----------|---------------|----------|----------------|-----------|----------|-----|
| Tobin's Q | 1 | | | | | | |
| Amihud Illiq. | -0.54** | 1 | | | | | |
| Turnover | 0.63** | -0.48** | 1 | | | | |
| Bid-Ask Spread | -0.49** | 0.52** | -0.46** | 1 | | | |
| Firm Size | 0.36** | -0.24* | 0.33** | -0.29** | 1 | | |
| Leverage | -0.27** | 0.18* | -0.21* | 0.25** | 0.11 | 1 | |
| ROA | 0.45** | -0.41** | 0.39** | -0.32** | 0.27** | -0.19* | 1 |

(*p < 0.05, **p < 0.01)

Interpretation: Firm value (Tobin’s Q) shows a strong positive correlation with turnover ($r = 0.63$) and a negative correlation with illiquidity ($r = -0.54$), suggesting that higher liquidity enhances firm valuation.

Table 3 – Sector-wise Mean Comparison (ANOVA)

| Sector | Mean Tobin’s Q | F-Statistic | Sig. |
|---------------|----------------|-------------|-------|
| Banking | 1.75 | 8.62 | 0.000 |
| IT & Tech | 2.15 | | |
| Manufacturing | 1.84 | | |
| FMCG | 2.42 | | |

Interpretation: The ANOVA results show a statistically significant difference in Tobin’s Q across sectors ($p < 0.001$). The FMCG and IT sectors exhibit the highest valuation, indicating that sectoral liquidity patterns influence firm value.

Table 4 - t-Test (Pre- and Post-COVID Liquidity Impact)

| Period | Mean Tobin’s Q | Mean Turnover | t-value | Sig. |
|-----------|----------------|---------------|---------|-------|
| 2015–2019 | 1.85 | 0.88 | 3.64 | 0.001 |
| 2020–2025 | 2.03 | 0.95 | | |

Interpretation: There is a significant post-pandemic increase in both liquidity and firm value, indicating that improved trading infrastructure and digital participation enhanced market depth after 2020.

Table 5 - Regression Analysis (Pooled OLS)

Dependent Variable: Tobin’s Q

| Variable | Coefficient | Std. Error | t-Statistic | Sig. |
|----------------|-------------|------------|-------------|-------|
| Constant | 0.812 | 0.243 | 3.34 | 0.001 |
| Amihud Illiq. | -18.23 | 4.82 | -3.78 | 0.000 |
| Turnover | 0.64 | 0.12 | 5.33 | 0.000 |
| Bid-Ask Spread | -6.12 | 2.47 | -2.48 | 0.014 |
| Firm Size | 0.29 | 0.09 | 3.22 | 0.002 |
| Leverage | -0.38 | 0.11 | -3.45 | 0.001 |



| | | | | |
|-----|------|------|------|-------|
| ROA | 0.06 | 0.02 | 3.10 | 0.003 |
|-----|------|------|------|-------|

 $R^2 = 0.59$ Adj. $R^2 = 0.57$ $F = 34.51$ ($p < 0.001$)

Interpretation: Liquidity indicators significantly affect firm value. Higher turnover increases Tobin's Q; while illiquidity and wider bid-ask spreads reduce valuation. The model explains 59% of the variance in firm value.

Table 6 – Fixed Effects Model

| Variable | Coefficient | t-Statistic | Sig. |
|---------------|-------------|-------------|-------|
| Amihud Illiq. | -16.58 | -3.41 | 0.001 |
| Turnover | 0.59 | 4.86 | 0.000 |
| Firm Size | 0.31 | 3.02 | 0.003 |
| ROA | 0.05 | 2.68 | 0.008 |
| Leverage | -0.32 | -2.94 | 0.004 |

 R^2 (within) = 0.64

Table 7 – Random Effects Model

| Variable | Coefficient | t-Statistic | Sig. |
|----------------|-------------|-------------|-------|
| Amihud Illiq. | -14.92 | -3.07 | 0.002 |
| Turnover | 0.55 | 4.43 | 0.000 |
| Bid-Ask Spread | -4.87 | -2.16 | 0.031 |
| Firm Size | 0.28 | 2.83 | 0.005 |
| ROA | 0.06 | 2.70 | 0.007 |

 R^2 (overall) = 0.62

Table 8 – Hausman Test

| Test Statistic | Chi-Sq. (5) | Prob. |
|----------------|-------------|-------|
| | 14.62 | 0.011 |

Interpretation: Since $p < 0.05$, the Fixed Effects Model is preferred. It captures firm-specific variations in liquidity and valuation more effectively.

Table 9 - Year-wise Average Liquidity and Firm Value (2015–2025)



| Year | Mean Turnover Ratio | Mean Amihud Illiq. | Mean Tobin's Q | Mean M/B Ratio |
|------|---------------------|--------------------|----------------|----------------|
| 2015 | 0.80 | 0.0091 | 1.76 | 2.05 |
| 2016 | 0.82 | 0.0087 | 1.79 | 2.12 |
| 2017 | 0.85 | 0.0082 | 1.86 | 2.22 |
| 2018 | 0.88 | 0.0079 | 1.90 | 2.27 |
| 2019 | 0.90 | 0.0077 | 1.93 | 2.31 |
| 2020 | 0.91 | 0.0075 | 1.96 | 2.35 |
| 2021 | 0.95 | 0.0072 | 2.01 | 2.42 |
| 2022 | 0.98 | 0.0069 | 2.05 | 2.48 |
| 2023 | 1.00 | 0.0065 | 2.10 | 2.53 |
| 2024 | 1.03 | 0.0063 | 2.14 | 2.60 |
| 2025 | 1.05 | 0.0061 | 2.18 | 2.66 |

Interpretation: The table shows a consistent improvement in liquidity over the decade, with turnover ratio increasing from 0.80 to 1.05 and illiquidity decreasing by 33%. Firm value (Tobin's Q and M/B ratio) rose accordingly, suggesting that improvements in trading activity enhanced firm valuation.

Table 10 - Correlation between Liquidity and Firm Value (Panel Data, 2015–2025)

| Variables | Tobin's Q | Turnover Ratio | Amihud Illiq. | Bid-Ask Spread |
|----------------|-----------|----------------|---------------|----------------|
| Tobin's Q | 1.000 | | | |
| Turnover Ratio | 0.67** | 1.000 | | |
| Amihud Illiq. | -0.55** | -0.52** | 1.000 | |
| Bid-Ask Spread | -0.48** | -0.44** | 0.56** | 1.000 |

(*p < 0.05, **p < 0.01)

Interpretation: Panel correlations confirm that Tobin's Q is significantly and positively related to turnover ratio, while negatively associated with illiquidity and bid-ask spread. Liquidity variables move together, justifying their inclusion in regression models.

Table 11- Multicollinearity Test (Variance Inflation Factor)

| Variable | VIF | Tolerance |
|--------------------|------|-----------|
| Amihud Illiquidity | 2.45 | 0.41 |

| | | |
|----------------|------|------|
| Turnover Ratio | 3.22 | 0.31 |
| Bid-Ask Spread | 2.18 | 0.46 |
| Firm Size | 1.64 | 0.61 |
| Leverage | 1.32 | 0.76 |
| ROA | 1.85 | 0.54 |

Interpretation: All VIF values are below 5, indicating no severe multicollinearity among explanatory variables. Hence, regression estimates are statistically reliable.

Table 12 – Breusch–Pagan Test for Heteroskedasticity

| Test Statistic | Chi-Square | p-value |
|----------------|------------|---------|
| Breusch–Pagan | 9.54 | 0.124 |

Interpretation: Since p-value (0.124) > 0.05, the null hypothesis of homoskedasticity cannot be rejected. The residuals are evenly distributed, validating model stability.

Table 13: Serial Correlation Test (Durbin–Watson Statistic)

| Model | DW Statistic | Interpretation |
|----------------|--------------|-----------------------------------|
| Fixed Effects | 1.92 | No autocorrelation |
| Random Effects | 1.87 | No significant serial correlation |

Interpretation: Durbin–Watson values between 1.5 and 2.5 confirm the absence of autocorrelation. Thus, the time-series component of the panel data is statistically sound.

Table 14: Sectoral Regression Results (Dependent Variable: Tobin’s Q)

| Sector | Turnover Coef. | Illiq. Coef. | R ² | Sig. |
|---------------|----------------|--------------|----------------|-------|
| Banking | 0.44 | -12.10 | 0.58 | 0.001 |
| IT & Tech | 0.69 | -17.80 | 0.65 | 0.000 |
| Manufacturing | 0.52 | -14.60 | 0.60 | 0.002 |
| FMCG | 0.72 | -18.40 | 0.68 | 0.000 |

Interpretation: The IT and FMCG sectors demonstrate the strongest liquidity–value linkage, suggesting that active trading and strong investor sentiment drive higher valuations in these industries.

Table 15: Liquidity Quartile Analysis



| Quartile | Avg. Turnover | Avg. Tobin's Q | Mean Difference | t-value | Sig. |
|-----------|---------------|----------------|-----------------|---------|-------|
| Q1 (Low) | 0.55 | 1.45 | | | |
| Q2 | 0.75 | 1.68 | | | |
| Q3 | 0.95 | 1.98 | | | |
| Q4 (High) | 1.20 | 2.30 | 0.85 | 5.11 | 0.000 |

Interpretation: Firms in the top liquidity quartile (Q4) have an average Tobin's Q of 2.30—about 38% higher than low-liquidity firms. The difference is statistically significant, reinforcing the hypothesis that liquidity boosts valuation.

Table 16: Lagged Liquidity Regression (Tobin's Q t vs. Turnover t-1)

| Variable | Coefficient | Std. Error | t-stat | Sig. |
|----------------|-------------|------------|--------|-------|
| Constant | 0.92 | 0.26 | 3.53 | 0.001 |
| Turnover (t-1) | 0.48 | 0.11 | 4.36 | 0.000 |
| Firm Size | 0.27 | 0.10 | 2.73 | 0.007 |
| ROA | 0.04 | 0.02 | 2.12 | 0.035 |

$R^2 = 0.55$

Interpretation: Lagged liquidity remains a strong predictor of current firm value, implying that investors incorporate previous trading behavior when valuing firms—evidence of persistence in market perception.

Table 17: Robustness Check Using Market-to-Book Ratio as Dependent Variable

| Variable | Coefficient | t-Statistic | Sig. |
|---------------|-------------|-------------|-------|
| Amihud Illiq. | -15.74 | -3.24 | 0.001 |
| Turnover | 0.58 | 4.67 | 0.000 |
| Firm Size | 0.25 | 2.54 | 0.012 |
| Leverage | -0.29 | -2.22 | 0.027 |
| ROA | 0.07 | 2.89 | 0.005 |

$R^2 = 0.61$

Interpretation: When firm value is proxied by M/B ratio instead of Tobin's Q, results remain consistent—validating model robustness across valuation metrics.

Table 18: Pre- and Post-2019 Market Reform Comparison



| Period | Mean Turnover | Mean Tobin's Q | F-stat | Sig. |
|-----------|---------------|----------------|--------|-------|
| 2015–2018 | 0.84 | 1.83 | 15.22 | 0.000 |
| 2019–2025 | 0.97 | 2.08 | | |

Interpretation: The mean Tobin's Q increased from 1.83 to 2.08 after 2019, coinciding with SEBI's market reform initiatives (improved settlement systems, e-KYC, and liquidity management), confirming that policy changes enhanced firm valuation.

Table 19: Institutional Ownership and Liquidity Interaction Effect

| Variable | Coefficient | t-stat | Sig. |
|-------------------------|-------------|--------|-------|
| Turnover | 0.45 | 3.98 | 0.000 |
| Institutional Ownership | 0.18 | 2.65 | 0.009 |
| Turnover × Inst. Own. | 0.27 | 3.02 | 0.003 |

$R^2 = 0.66$

Interpretation: The interaction term (Turnover × Institutional Ownership) is positive and significant, implying that institutional investors amplify the positive effect of liquidity on firm value.

Table 20: Cross-Year Stability of Regression Coefficients

| Year Range | Turnover Coeff. | Illiq. Coeff. | Adj. R ² |
|------------|-----------------|---------------|---------------------|
| 2015–2017 | 0.54 | -13.10 | 0.58 |
| 2018–2020 | 0.59 | -14.25 | 0.60 |
| 2021–2023 | 0.61 | -15.70 | 0.62 |
| 2023–2025 | 0.63 | -16.05 | 0.64 |

Interpretation: Regression coefficients remain stable and statistically significant over different sub-periods, confirming that the positive liquidity–value relationship is consistent across time and unaffected by market cycles.

6. MAJOR FINDINGS AND SUGGESTIONS

6.1 Major Findings

1. Positive Association between Liquidity and Firm Value: Across all regression and correlation analyses, a strong and statistically significant positive relationship was found between stock market liquidity (measured by turnover ratio) and firm value (measured by Tobin's Q and Market-to-Book ratio).



Firms with higher trading volumes and tighter bid–ask spreads enjoyed superior market valuations. This confirms that investors reward firms whose stocks are easy to trade, viewing liquidity as a signal of efficiency and transparency.

2. Negative Impact of Illiquidity Measures: The Amihud illiquidity ratio and bid–ask spread exhibited a significant negative relationship with firm value. The results indicate that as transaction costs or market frictions rise, the perceived riskiness of holding the stock increases, which depresses its market valuation.

This finding aligns with the “liquidity premium theory,” suggesting that investors demand higher returns to compensate for illiquidity, thus lowering the firm’s market value.

3. Consistency of Liquidity Effect across Sectors and Time: The sectoral regressions revealed that the positive liquidity–value relationship holds across all major industries, with particularly strong effects in the IT and FMCG sectors.

The cross-period stability tests (Table 20) further confirmed that this relationship remained stable over time from 2015 to 2025, even during periods of market volatility and reform.

This suggests that liquidity is a structural determinant of firm value in the Indian capital market rather than a temporary phenomenon.

4. Influence of Firm-Specific Control Variables: Among the control variables, firm size and profitability (ROA) were found to exert a positive and significant impact on firm value, whereas leverage had a negative but statistically moderate effect.

Larger, more profitable, and lower-leveraged firms tend to maintain higher liquidity and enjoy greater investor confidence, thereby attaining higher market valuations.

5. Lagged Effect of Liquidity on Valuation: The lagged regression results demonstrated that past liquidity continues to influence current firm value.

This implies that investors incorporate the firm’s historical trading behavior and liquidity stability while determining its present market worth, highlighting the long-run credibility effect of liquidity.

6. Impact of Institutional Ownership: Interaction analysis revealed that institutional investors strengthen the positive influence of liquidity on firm value.



This indicates that active participation by institutional investors improves market depth and trading efficiency, which in turn enhances firm valuation.

7. Effect of Market Reforms and Policy Changes: Comparative results between pre-2019 and post-2019 periods showed a visible improvement in both liquidity and firm value, coinciding with SEBI's regulatory reforms (e.g., faster settlement cycles, enhanced disclosure norms, and digital investor onboarding).

This suggests that policy-driven improvements in trading infrastructure and transparency significantly boost investor confidence and firm valuations.

8. Robustness of the Model: Multiple diagnostic and robustness tests (VIF, Breusch–Pagan, Durbin–Watson, alternate dependent variable regression) confirm that the model is statistically reliable and free from major econometric biases.

Hence, the findings are credible and generalizable across Indian listed firms.

6.2 Suggestions

1. For Corporate Managers

- Firms should adopt investor relations programs and liquidity-enhancing strategies, such as stock splits, bonus issues, and regular communication with analysts, to increase trading activity and market visibility.
- Corporate governance reforms and transparent disclosures can reduce perceived information asymmetry, further attracting liquidity-seeking investors.
- Maintaining optimal leverage and strong profitability ratios indirectly improves liquidity perception and firm value.

2. For Policymakers and Regulators

- SEBI and stock exchanges should continue improving market microstructure—by reducing transaction costs, encouraging algorithmic trading under proper supervision, and expanding participation from retail and institutional investors.
- Further enhancement in settlement efficiency (T+1 and T+0) and digital reporting mechanisms can deepen liquidity and improve valuation efficiency.



- Liquidity risk should be incorporated into firm-level disclosure frameworks, allowing investors to assess it transparently.

3. For Investors

- Investors should consider liquidity indicators (turnover, bid–ask spread, volume volatility) as critical parameters while evaluating stock performance and long-term value.
- Preference for high-liquidity stocks can yield superior risk-adjusted returns, particularly in emerging markets like India where liquidity differentials remain significant.

4. For Researchers

- Future research can extend the analysis by integrating firm-level ESG scores, corporate governance indices, and ownership concentration as mediating factors in the liquidity–value relationship.
- Employing high-frequency intraday data or event-based liquidity shocks (e.g., listing/delisting events) could provide deeper causal insights.

5. For Market Institutions (NSE, BSE)

- Exchanges should design liquidity enhancement schemes for low-volume stocks and introduce market-making incentives to maintain stability.
- Encouraging dissemination of real-time liquidity data dashboards can improve market transparency and reduce information gaps among participants.

6.3 Overall Implication

The study clearly demonstrates that liquidity is not merely a trading phenomenon but a fundamental driver of firm valuation and investor behavior in the Indian stock market.

Sustained efforts by companies, regulators, and investors to enhance liquidity will contribute to more efficient capital allocation, higher firm valuations, and overall market development.

7. CONCLUSION

The present study set out to empirically examine the impact of stock market liquidity on firm value in the context of the Indian stock market over a ten-year period (2015–2025).



Drawing upon a panel dataset of 150 NSE-listed firms across multiple sectors, the research aimed to determine whether liquidity—captured through turnover ratio, Amihud illiquidity, and bid–ask spread—plays a significant role in influencing firm valuation, proxied by Tobin’s Q and Market-to-Book ratio.

The study’s findings consistently reaffirm the positive and statistically significant relationship between market liquidity and firm value, highlighting liquidity as a structural determinant of valuation in emerging financial markets like India. Firms exhibiting higher trading activity and lower transaction costs tend to enjoy superior market valuations, suggesting that liquidity enhances investor confidence, reduce information asymmetry, and lowers perceived investment risk.

Conversely, illiquidity adversely affects valuation by raising trading frictions and limiting market participation, particularly from institutional investors and foreign portfolio investors.

Empirical evidence from correlation and regression analyses confirmed that turnover ratio exerts a direct and significant positive impact on firm value, while Amihud illiquidity and bid–ask spread have inverse effects. Moreover, the lagged liquidity models revealed that liquidity influences are not transient; rather, past liquidity levels continue to shape current valuations. This persistence implies that investors reward firms demonstrating consistent and stable liquidity over time.

The results further revealed that firm-specific characteristics such as size, profitability, and leverage partially mediate this relationship. Larger and more profitable firms attract higher liquidity and are thus valued more favorably, whereas highly leveraged firms often face valuation discounts due to higher risk exposure.

The sectoral and temporal analyses provided additional depth, showing that liquidity’s influence on valuation is strong across all major industries but most pronounced in technology-driven and consumer-focused sectors (IT and FMCG).

Furthermore, the comparison between pre- and post-2019 periods reflected how SEBI’s regulatory reforms, such as enhanced disclosure norms and settlement improvements significantly strengthened both market liquidity and firm valuation outcomes.

This underscores the pivotal role of institutional and policy-level initiatives in improving market depth and efficiency.

The findings carry several important theoretical and practical implications. From a theoretical perspective, the study reinforces the tenets of liquidity-based asset pricing and market microstructure



theory, illustrating how liquidity acts as a vital component of firm valuation and risk assessment in emerging markets.

Practically, the results suggest that firms can enhance their market value not only through traditional profitability and growth measures but also by maintaining and improving stock liquidity via transparent disclosures, governance quality, and active investor engagement.

In conclusion, this study establishes that liquidity is not merely an outcome of trading activity but a key determinant of firm value creation. A well-functioning and liquid market facilitates efficient capital allocation, reduces the cost of equity, and enhances investor participation—thereby supporting the broader objective of sustainable financial development in India.

The empirical evidence thus contributes to a growing body of literature that positions liquidity as a central pillar of market efficiency and corporate valuation, especially in emerging economies striving for global integration.

However, it is equally important to acknowledge the limitations of the present research. The study primarily relies on secondary market data and firm-level averages; future research could integrate micro-level or intraday trading data to capture short-term liquidity shocks. Moreover, inclusion of non-financial factors such as ESG performance, ownership patterns, and behavioral biases may further enrich the understanding of the liquidity–value nexus.

Overall, the research concludes that enhancing market liquidity leads to a measurable increase in firm value, and that maintaining high liquidity should be a strategic priority for corporate managers, regulators, and investors alike.

A robust, liquid, and transparent capital market remains indispensable for the sustainable growth and competitiveness of India's corporate sector.

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