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The Impact of Government Policies and Related Factors on Stock Prices

Linkun Yu*

Shenzhen Senior High School, Shenzhen, Guangdong, 518000, China

*yildiz0121yu@gmail.com

Abstract

Stock price fluctuations are closely related to national macro policies. As core regulatory tools, fiscal and monetary policies have their mechanisms and implementation effects under intense academic and market scrutiny. This paper conducts research on the impact of government policies and related factors on stock prices. By employing literature review, comparative analysis, and logical analysis, it systematically dissects the action paths of fiscal and monetary policies, explores the policy synergy effects and the influence of market expectations and investor sentiment, and combines practical cases to analyze their application in investor decision-making and corporate planning. The research finds that the impact of policies on stock prices is not the result of a single factor but rather a product of the characteristics of policy tools, industry heterogeneity, market expectations, and cyclical environments. The findings of this paper can enrich the theoretical system of the interaction between financial markets and policies, provide decision-making references for investors, offer a basis for policymakers to optimize policy directions, and assist listed companies in responding to policy environments and improving the healthy development mechanism of capital markets.

Keywords

Government Policies; Stock Price Fluctuations; Fiscal Policies; Monetary Policies; Policy Coordination.

1. Introduction

In the operation of the financial market, fluctuations in stock prices not only reflect changes in market supply and demand but are also closely related to the country's macroeconomic policies. Fiscal policy and monetary policy, as the core means for the government to regulate the economy, act on the stock market through various transmission channels. Their implementation effects directly influence the trend of stock prices. Meanwhile, the synergy between policies can further amplify or weaken their impact on the market. With the continuous development of the financial market, the investor structure has become increasingly complex. Market expectations and investor sentiment have also become important variables affecting stock prices, making the mechanism by which policies influence stock prices more diverse.

From a theoretical perspective, although existing studies on the relationship between macro policies and stock prices have established a certain framework, they mostly focus on a single policy tool or static synergy effects. There is still a need for further exploration of the dynamic adjustment mechanisms of policies in different market environments and the interaction of multiple factors. From a practical standpoint, investors need to formulate reasonable investment strategies based on policy trends, policy makers need to clearly define the direction of policy optimization to stabilize the market, and listed companies need to adjust their business plans in accordance with the policy environment. Therefore, in-depth research on the

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impact of government policies and related factors on stock prices has both significant theoretical significance and practical value. Based on the above reasons, this paper takes the impact of government policies and related factors on stock prices as the research topic, aiming to reveal its internal mechanism of action and provide more comprehensive references for market participants.

2. Literature Review

2.1. The Impact of Monetary Policy on Stock Prices

Monetary policy mainly affects stock prices through measures such as interest rate adjustments and liquidity control. Huayu Fei found that when a reduction in interest rates and an increase in market money supply create a synergy effect, the policy's boosting effect on stock prices is more significant [1]. For instance, during the global financial crisis in 2008, the series of monetary policies implemented by the United States, with clear goals and closely coordinated tools, effectively helped the stock market stabilize and recover. On the contrary, if there are conflicts in policy goals, such as simultaneous interest rate hikes and monetary easing, it may lead to significant fluctuations in stock prices. The studies by Broda and Romalis have confirmed that in some emerging markets, due to the improper coordination of monetary and exchange rate policies, stock prices have dropped significantly [2].

For the Chinese market, Xu Wei and Ji Yufeng found that the transmission mechanisms of money supply and interest rate adjustments on stock prices vary in different periods, and market expectations play an important intermediary role [3]. Ma Yong and Chen Yulu pointed out that different industries have heterogeneous responses to monetary policies, and the stock prices of growth-oriented industries such as technology are more sensitive to policy changes [4]. Additionally, Bao Pengzhi's research shows that the improvement of central bank policy transparency helps stabilize stock price fluctuations and reduces irrational market reactions [5].

2.2. The Impact of Fiscal Policy on Stock Prices

Fiscal policies influence stock prices through tools such as tax incentives and government spending, and there are structural differences in their effects on different industries. Fama argued that when tax relief for manufacturing industries is implemented simultaneously with infrastructure investment, the compatibility between the policy and industry demand increases, and the stock prices of cyclical industries such as steel and machinery rise significantly above the market average [6]. However, Ljungqvist and Smolyansky proposed that if tax incentives are biased towards high-energy-consuming industries, and conflict with the "dual carbon" goals, it may trigger market concerns about the sustainability of the policy, leading to pressure on the stock prices of related industries [7].

The cases of China's new energy industry provide strong evidence for the impact of fiscal policies on stock prices. Meng Xiaokai found that the combined implementation of fiscal subsidies and research funding led to a significantly longer duration of positive stock price responses for the relevant enterprises compared to the implementation of a single subsidy policy [8]. Smith and Jones's cross-national study confirmed that the greater the diversity and precision of fiscal policy tools, the more effectively they can stabilize industry stock prices [9]. Meanwhile, Wang Yu and Li Hongjin discovered that announcing clear fiscal stimulus plans in advance can guide the market to form stable expectations, prompting the stock prices of related industries to show positive reactions earlier [10].

2.3. The Impact of Policy Synergy on Stock Prices

The coordinated implementation of fiscal policy and monetary policy has a special impact on stock prices. Bernanke and Blinder pointed out that when fiscal expansion and monetary easing

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are carried out simultaneously, the combined effect of the two often drives stock prices to rise significantly [11]. In 2024-2025, China's macro policies focused on promoting stable growth. The coordinated effect of fiscal and monetary policies began to emerge. The central bank launched tools to support the stability of the capital market, and the Ministry of Finance introduced incremental fiscal policies, which led to a general rise in the A-share market after the end of September 2024.

However, policy coordination also faces challenges. Li Xunlei believes that if policy coordination is not handled properly, such as having problems in terms of force balance or implementation timing, it may lead to the cancellation of each other's effects, making it difficult to effectively stabilize stock prices [12]. Xu Wei and Ji Yufeng as well as Zhou Junmei further pointed out that in different economic cycles, the optimal coordination model of fiscal and monetary policies varies, and it is necessary to adjust dynamically according to the economic environment [13,14].

2.4. The Influence of Market Expectations and Investor Sentiment on Stock Prices

The influence of market expectations and investor sentiment on stock prices has been extensively studied. Behavioral finance theory suggests that emotions can cause stock prices to deviate from their fundamental values, and market expectations directly or indirectly affect stock prices by influencing investment decisions. Baker and Wurgler confirmed that an elevated mood would push up stock prices and trigger subsequent reversals. In domestic research, Tang Yiming and Zhang Qiang using the VAR model discovered an interaction between emotions and returns, and emphasized that there is a bidirectional influence between the two [15,16,17]. Reference pointed out that the impact of emotions is asymmetric in bull and bear markets, either manifesting as a stronger impact in bear markets or showing a difference in predictive power [18,19].

Furthermore, market expectations and investor sentiment also influence each other. Optimistic expectations often accompany elevated sentiment to jointly drive up stock prices; conversely, they can exacerbate declines. Although existing studies have affirmed the importance of both, there is still room for further exploration in terms of the details of the influencing mechanism and the precision of quantification.

2.5. Summary of Literature Review

In conclusion, fiscal policies, monetary policies, and investor sentiment factors influence stock prices through their respective transmission channels. Meanwhile, the suitability of policy tools, the timing of implementation, and the degree of coordination directly determine the effect. Current research has revealed the differences in the impact of single policies and policy combinations on stock prices. However, the dynamic adjustment mechanism of policy coordination in different market environments, as well as the exploration of the interaction of policy tool characteristics, industry heterogeneity, market expectations, and cyclical environments, still require further investigation. This also provides a direction for our research.

3. Main Text Analysis

3.1. Analysis of the Pathway by Which Government Policies Affect Stock Prices

The government exerts significant influence on stock price trends through two core tools - fiscal policy and monetary policy - in various dimensions such as corporate profit expectations, market liquidity, investor sentiment and confidence.

In terms of fiscal policy, the adjustment of tax policies has a direct and significant impact on stock prices. A reduction in corporate income tax can directly increase the after-tax profits of enterprises, improve the market's expectations for the enterprises' earnings, and thereby drive

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stock prices to rise; tax exemption for value-added tax can alleviate the cash flow pressure of enterprises and enhance their market competitiveness, also having a positive effect on stock prices. The direction of government spending will also guide stock price fluctuations. When infrastructure investment increases, the order and revenue expectations of upstream industries such as construction and steel rise, and the stock prices of related enterprises rise accordingly; an increase in spending in the social welfare sector can promote consumption, benefiting stocks of consumption-related companies. In addition, industrial support policies such as subsidies for new energy vehicles and research and development subsidies can enhance the growth expectations of the industry and push up the stock prices of related enterprises.

Monetary policy mainly affects stock prices through interest rate adjustments and management of money supply. Lowering interest rates not only reduces the financing costs for enterprises, expands their profit margins, but also guides funds to shift from savings to the stock market, increasing market liquidity. Under the combined effect of these two factors, stock prices rise; conversely, raising interest rates will increase the financing costs for enterprises, restrain the inflow of funds into the stock market, and lead to a decline in stock prices. In terms of money supply, the growth of M2 injects more liquidity into the market, making market funds abundant and conducive to the rise of stock prices; while tightening money supply will cause a shortage of funds in the stock market, making stock prices prone to decline.

3.2. The Impact of Policy Coordination and Related Factors on Stock Prices

The synergy of policies cannot be ignored in terms of its impact on stock prices. When fiscal policies and monetary policies are in the same direction, such as when fiscal expansion and monetary easing are implemented simultaneously, it will strengthen positive market expectations and amplify the driving effect on stock prices; if there is a conflict between policies, such as when fiscal contraction and monetary easing occur concurrently, it will cause the market to be confused, weaken the impact of policies on stock prices, and even trigger stock price fluctuations.

Market expectations are significantly influenced by policy transparency and predictability. Clear and stable policy signals, such as explicit industrial planning and gradual tax rate adjustments, can enable investors to form rational profit and valuation expectations, smoothing out stock price fluctuations; while ambiguous and frequently changing policies will trigger market concerns, intensifying stock price volatility. Investor sentiment will also convey the impact of policies. If the market develops an optimistic mood due to good policy synergy, it will further boost stock prices; if pessimism arises due to policy conflicts and is continuously passed on in the market, it will further amplify the negative effect of policies on stock prices.

Specifically, investor sentiment can be reflected through various indicators, such as the discount rate of closed-end funds, the dividend premium (the valuation difference between high-dividend stocks and low-dividend stocks), the turnover rate, and the proportion of equity financing (the proportion of stock financing in total financing). These indicators can provide different perspectives to reflect the changes in market investors' sentiment, thereby assisting in predicting the possible trend of stock prices.

3.3. The Application of Policies and Related Factors in Practice

3.3.1. Application in Investor Decision-Making

Investors can analyze the direction of government policies to predict stock trends and formulate reasonable investment strategies. For instance, when observing that the government's support for the new energy industry is continuously increasing, they can purchase stocks related to the new energy sector in advance to gain the benefits brought by the favorable policies; when expecting a tightening of monetary policy, they should reduce the

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holdings of high-valued and highly sensitive to capital stocks to avoid the risk of stock price decline.

At the same time, investors can utilize policy influencing factors and model construction to formulate investment strategies. By applying the event study method, they can seize trading opportunities brought about by short-term policy benefits. Based on the results of panel regression analysis, they can allocate resources to industries and enterprises that are certain to benefit from policies. Taking the disclosure of securities performance forecasts in 2025 as an example, at that time, due to the "realization of benefits", stock prices were under pressure, and the comprehensive strengthening of regulation made market sentiment cautious. If investors can combine market expectations and sentiment factors, and not merely rely on performance growth, but also consider the sustainability of profits, the degree of previous market sentiment release, and policy orientation, they can make more rational decisions and avoid losses in the investment of securities companies due to the deviation between stock prices and performance.

3.3.2. Application in Enterprise Planning

Enterprises can adjust their business strategies in accordance with policy guidance to adapt to market changes and enhance their own value. When tax incentives are inclined towards innovation and research and development, enterprises increase their investment in research and development. This not only enables them to comply with the policies to obtain tax deductions and reduce operating costs, but also enhances their technological competitiveness, thereby driving up stock prices and facilitating enterprises' refinancing and long-term development.

Take Yilirong Co., Ltd. as an example. Its new controller, Zhang Yuan, leveraging his connections in the consumer electronics sector, helped the company enter the supply chains of related enterprises such as OPPO and VIVO, forming a "automobile + 3C" dual-drive model. This company achieved strategic transformation and value enhancement by responding to market expectations and sentiments, changing the market's perception of its traditional cyclical stocks, effectively boosting the company's valuation, and providing a reference for other enterprises to cope with policy environment changes.

3.4. The Future Research Direction on the Impact of Government Policies and Related Factors on Stock Prices

Future research can incorporate machine learning algorithms (such as artificial intelligence deep learning) to process a large amount of policy texts and market sentiment data, more accurately identifying the potential factors and nonlinear relationships that influence stock prices, thereby enhancing the accuracy and depth of the research. At the same time, integrating blockchain data to obtain the real transaction and financing information of enterprises can reduce the impact of data distortion on research results, further improving the accuracy of policy impact factor measurement, and providing more reliable theoretical support for policy formulation, investor decision-making, and enterprise planning.

4. Conclusion

This article conducts a study on the impact of government policies and related factors on stock prices, and reaches the following conclusions: First, fiscal policies and monetary policies affect stock prices through different channels. Tax adjustments, government expenditures, and industrial support policies in fiscal policies, as well as interest rate adjustments and money supply management in monetary policies, all exert influence on stock prices from dimensions such as corporate profits and market liquidity. Second, the policy synergy effect is significant. When fiscal and monetary policies have the same direction, they can amplify the driving effect on stock prices. Policy conflicts will weaken the policy effect, and the optimal policy synergy

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mode varies in different economic cycles. Third, market expectations and investor sentiment are crucial in influencing stock prices. Policy transparency and predictability affect market expectations, which in turn act on stock prices. Investor sentiment also conveys and amplifies the impact of policies on stock prices. Fourth, the influence of policies on stock prices is not the result of a single effect. It is the product of the joint action of policy tool characteristics, industry heterogeneity, market expectations, and cyclical environment.

This study enriches the theoretical framework of the interaction between the financial market and policies, expands the interdisciplinary research perspective, and reveals the theoretical value of the uniqueness of emerging markets. In practice, it can provide decision-making references for investors, helping them formulate reasonable investment strategies based on policies and related factors; it can also provide an optimization direction for policy makers, assisting them in dynamically adjusting policies according to the market environment and maximizing the policy synergy effect; it can help listed companies better cope with the policy environment, adjust their business plans, enhance enterprise value, and thereby improve the healthy development mechanism of the capital market.

However, this study still has certain limitations. For instance, it did not conduct an in-depth analysis of the quantitative degree of the impact of policies on stock prices. In the future, quantitative models can be further introduced, combined with more diverse data, to accurately calculate the extent of the impact of different policies and related factors on stock prices, providing more accurate references for market participants.

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