

Design and Implementation of Household Appliances Control Using GSM

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Abstract : In this paper, designing and implementing GSM-Based control of Electrical Household Appliances is presented. The issues of paying high electricity bills generated due to household Electrical & Electronic appliances at home/office is alarming. To help deduct the total number of energy use and amount to be spent on electricity bills, GSM-Based control of Electrical Household Appliances is proposed. The system is designed to allow the consumer to control the switching ON/OFF of his/her electrical and electronics home appliances via mobile phone from anywhere at any time. The system implemented with help of arduino hardware and GSM module software. Any household appliances could be switched ON by clicking a Tab in the Consumer's mobile phone, that signal send to the receiver panel at home, the receiver antenna picks the signal and forward it to microcontroller which decodes the keywords and command the instructions to trigger any device connected to the system ports. If the device (s) is/are switched ON, then the smart phone tab shows the the status of system with green mark. Similarly if the Device is Switched OFF then the smart phone Tab shows Red mark. The system is implemented, program written and tested with accurate result.

IndexTerms - GSM, Arduino, Relay coils .

1.INTRODUCTION

We come across many situations in life where we see one of our family member comes to a stage when they can't take care of themselves due to old age or any other chronic health issues, and the members of the family aren't in a position to be able to dedicate the time and energy required to take care of a bed ridden person due to the hectic schedule of today's work environment. This leads them to go for alternative option like transferring them to a facility which could be devastating consequence on the family member thus opting for a care taker who could meet the needs of them and reduced the pressure of responsibility on the wards of the family. Due to this they keep the caretakers to see the requirements for the old people. In some cases caretakers are busy in their work like cleaning the house, going to market in that time calling the caretaker for normal functions like close the door, adjusting the room temperature. Overloading work on the caretaker might cause resentment leading to tension between them.

Sometimes old people may get guilty and depressed for their inability to do their own simple work. So in order to help them we are introducing the home automation by using google assistant. By using this setup we can help them to do their own simple works. In this concept we are trying to provide the senior citizen to do menial works on their own.

This set up not only helps senior citizens but also to the bed ridden and differently-abled people. The main theme of the paper is to help the persons who are depend on others for their requirements. But for the sake of convenience we are representing certain applications for senior citizens who are bed ridden.

Here we are using **GSM BASED PHONE** A Mobile phone is a revolutionary invention of the century. It was primarily designed for making and receiving calls & text messages, but it has become the whole world after the Smart phone comes into the picture. In this paper we are building a home automation system, where one can control the home appliances, using the simple **GSM based phone**, just by sending SMS through his phone. In this paper, no Smart phone is needed, just the old GSM phone will work to switch ON and OFF any home electronic appliances, from anywhere.

2. LITERATURE REVIEW

In this section, discussed different Home Automation System with their technology with features, benefit and limitations they have. The Home automation system that uses Wi-Fi technology [1]. System consists of three main components; web server, which presents system core that controls, and monitors users' home and hardware interface module(Arduino PCB (ready-made), Wi-Fi shield PCB, 3 input alarms PCB, and 3 output actuators PCB.), which provides appropriate interface to sensors and actuator of home automation system. The System is better from the scalability and flexibility point of view than the commercially available home automation systems. The User may use the same technology to login to the server web based application. If server is connected to the internet, so remote users can access server web based application through the internet using compatible web browser.

Shih-Pang Tseng et al. [2] proposed Smart House Monitor & Manager (SHMM), based on the ZigBee, all sensors and actuators are connected by a ZigBee wireless network. They designed a simple smart socket, which can remote control via ZigBee. PC host is used as a data collector and the motion sensing, all sensing data are transferred to the VM in the cloud. The user can use the PC or Android phone to monitor or control through the Internet to power-saving of the house

Arduino microcontroller to receive user commands to execute through an Ethernet shield. Our house network used together both wireless ZigBee and wired X10 technologies [3]. This system followed smart task scheduling with a heuristic for the Resource-constrained-scheduling problem (RCPSP). The mobile device can be either wired to the central controller through USB cable or communicates with it wirelessly, within the scope of the home. Arduino contains the web server application that communicates through the HTTP protocol with Web-based Android application. The system is highly flexible and scalable and expandable.

PIC16F887 microcontroller for home appliances controls with GSM for control of the appliances. [4]. It has high availability, coverage and security but the cost of SMS. AT commands can be sent through the GSM network to controls the home devices. The system does not does not have anystate information related to the devices and expects the user to keep track of it.

Arduino board is the controller used to control the appliances by using GSM technology. It uses certain peripheral drivers and relays to achieve this interfacing. The application on smartphone generates SMS messages based on the user commands and sends it to the GSM modem attached to the Arduino and control the home appliances [5]. The system has drawbacks of cost and reliability of SMS. An interface cannot be customized based on devices.

It has been designed Arduino board with Bluetooth board were developed for home automation [6]. Python program is used on the cell phone to provide the user interface. The Bluetooth board has I/O ports and relays are used for interfacing with the devices which are to be controlled and monitor. The Bluetooth is password protected to ensure that the system is secure from intruders. The Bluetooth has a range of 10 to 100.

3.PROPOSED METHOD

The system proposed in [1] provides 3 means to control the home: the GSM network, the Internet and through speech. The real time monitoring has been an important feature that can be used in the home automation systems. As a change in the status of the devices occurs, the user can be informed in real time. The user commands are transferred to a server which is usually done by a PC. The server processes the user commands and sends them to the relevant units. This can help control the appliances. GSM is used as a communication medium to help establish connection in places where there may not be proper internet connectivity. The server uses AT commands to communicate with the GSM modem. The mobile interface is developed using J2ME. The server has 4 engines running – the web server, database, main control program and speech recognition program. The system can be controlled using SMS. It can send confirmation messages. Speech processing is done with a dynamic time wrapping algorithm. The voice activation has been tested and found to be too impractical. As a more stable alternative, the voice input can be activated through a wireless unit the user carries along in the house. Each application node has four parts – the transmitter, receiver, I/O device and a microcontroller. The main control program in the server takes status information from the devices' transceiver in real time

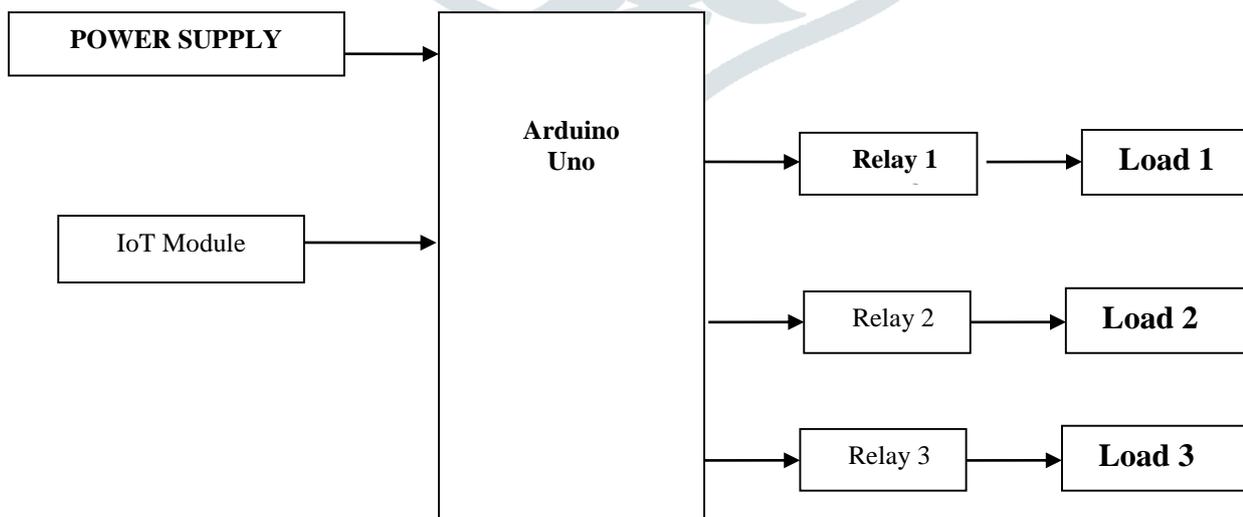


Figure 3.1:GSM Based Home automation using Ardurio model

The Block diagram Shows that the paper we are building a home automation system, where one can control the home appliances, using the simple **GSM based phone**, just by sending SMS through his phone. In this paper, no Smart phone is

needed, just the old GSM phone will work to switch ON and OFF any home electronic appliances, from anywhere. In this paper, **Arduino** is used for controlling whole the process. Here we have used GSM wireless communication for controlling home appliances. We send some commands like “#A.light on*”, “#A.light off*” and so on for controlling AC home appliances. After receiving given commands by Arduino through GSM, Arduino send signal to relays, to switch ON or OFF the home appliances using a relay driver.

We come across many situations in life where we see one of our family member comes to a stage when they can't take care of themselves due to old age or any other chronic health issues, and the members of the family aren't in a position to be able to dedicate the time and energy required to take care of a bed ridden person due to the hectic schedule of today's work environment.

4.HARDWARE REQUIREMENTS

This can help you to access your home when you are out . You can switch on and off the home appliances from anywhere. The following important hardware to be implemented in the design of proposed system.

- ATMEGA328P Microcontroller
- GSM module
- Arduino Uno
- Relay Board

4.1 ATMEGA328P MICROCONTROLLER

The Atmel 8-bit AVR RISC-based microcontroller combines 32 kB ISP flash memory with read-while-write capabilities, 1 kB EEPROM, 2 kB SRAM, 23 general purpose I/O lines, 32 general purpose working registers, three flexible timer/counters with compare modes, internal and external interrupts, serial programmable USART, a byte-oriented 2-wire serial interface, SPI serial port, 6-channel 10-bit A/D converter (8-channels in TQFP and QFN/MLF packages), programmable watchdog timer with internal oscillator, and five software selectable power saving modes. The device operates between 1.8-5.5 volts. The device achieves throughput approaching 1 MIPS per MHz

4.2 GSM MODULE

GSM is a mobile communication modem; it stands for global system for mobile communication (GSM). The idea of GSM was developed at Bell Laboratories in 1970. It is widely used mobile communication system in the world. GSM is an open and digital cellular technology used for transmitting mobile voice and data services operates at the 850MHz, 900MHz, 1800MHz and 1900MHz frequency bands.

GSM system was developed as a digital system using time division multiple access (TDMA) technique for communication purpose. A GSM digitizes and reduces the data, then sends it down through a channel with two different streams of client data, each in its own particular time slot. The digital system has an ability to carry 64 kbps to 120 Mbps of data rates.



FIGURE 4.1 GSM Module inside the board

TDMA technique relies on assigning different time slots to each user on the same frequency. It can easily adapt to data transmission and voice communication and can carry 64kbps to 120Mbps of data rate.

From the below circuit, a GSM modem duly interfaced to the MC through the level shifter IC Max232. The SIM card mounted GSM modem upon receiving digit command by SMS from any cell phone send that data to the MC through serial communication. While the program is executed, the GSM modem receives command 'STOP' to develop an output at the MC, the contact point of which are used to disable the ignition switch. The command so sent by the user is based on an intimation received by him through the GSM modem 'ALERT' a programmed message only if the input is driven low. The complete operation is displayed over 16x2 LCD display.

4.3 ARDUINO IDE

Arduino is an open-source electronics platform based on easy-to-use hardware and software. Arduino boards are able to read inputs - light on a sensor, a finger on a button, or a Twitter message - and turn it into an output - activating a motor, turning on an LED, publishing something online. You can tell your board what to do by sending a set of instructions to the microcontroller on the board. To do so you use the Arduino programming language (based on Wiring), and the Arduino Software (IDE), based on Processing.

Over the years Arduino has been the brain of thousands of papers, from everyday objects to complex scientific instruments. A worldwide community of makers - students, hobbyists, artists, programmers, and professionals - has gathered around this open-source platform, their contributions have added up to an incredible amount of accessible knowledge that can be of great help to novices and experts alike.

Arduino was born at the Ivrea Interaction Design Institute as an easy tool for fast prototyping, aimed at students without a background in electronics and programming. As soon as it reached a wider community, the Arduino board started changing to adapt to new needs and challenges, differentiating its offer from simple 8-bit boards to products for IoT applications, wearable, 3D printing, and embedded environments. All Arduino boards are completely open-source, empowering users to build them independently and eventually adapt them to their particular needs. The software, too, is open-source, and it is growing through the contributions of users worldwide.

4.4 BOARD TYPES:

Various kinds of Arduino boards are available depending on different microcontrollers used. However, all Arduino boards have one thing in common: they are programmed through the Arduino IDE. The differences are based on the number of inputs and outputs (the number of sensors, LEDs, and buttons you can use on a single board), speed, operating voltage, form factor etc. Some boards are designed to be embedded and have no programming interface (hardware).

4.4.1 ARDUINO BOARD DESCRIPTION

We will learn about the different components on the Arduino board. We will study the Arduino UNO board because it is the most popular board in the Arduino board family. In addition, it is the best board to get started with electronics and coding. Some boards look a bit different from the one given below, but most Arduino's have majority of these components in common.

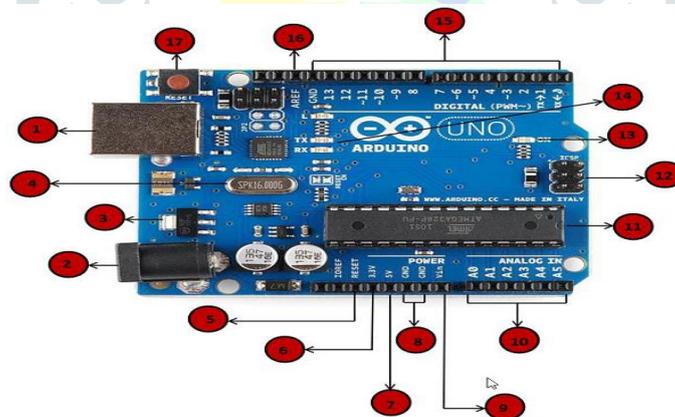


FIG 4.2 ARDUINO BOARD

4.5 CHANNEL RELAY BOARD:

This is a LOW Level 5V 2-channel relay interface board, and each channel needs a 15-20mA driver current. It can be used to control various appliances and equipment with large current. It is equipped with high-current relays that work under AC250V 10A or DC30V 10A. It has a standard interface that can be controlled directly by microcontroller. This module is optically isolated from high voltage side for safety requirement and also prevent ground loop when interface to microcontroller.



Fig 4.5.2 Channel Relay Board

VCC and RY-VCC are also the power supply of the relay module. When you need to drive a large power load, you can take the jumper cap off and connect an extra power to RY-VCC to supply the relay; connect VCC to 5V of the MCU board to supply input signals. NOTES: If you want complete optical isolation, connect "Vcc" to Arduino +5 volts but do NOT connect Arduino Ground. Remove the Vcc to JD-Vcc jumper. Connect a separate +5 supply to "JD-Vcc" and board Gnd. This will supply power to the transistor drivers and relay coils. If relay isolation is enough for your application, connect Arduino +5 and Gnd, and leave Vcc to JD-Vcc jumper in place.

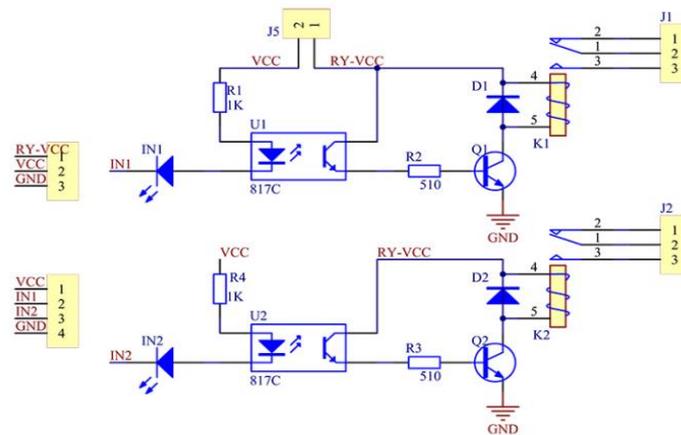


FIG 4.3 Schematic of Channel relay

It is sometimes possible to use this relay boards with 3.3V signals, if the JD-VCC (Relay Power) is provided from a +5V supply and the VCC to JD-VCC jumper is removed. That 5V relay supply could be totally isolated from the 3.3V device, or have a common ground if opto-isolation is not needed. If used with isolated 3.3V signals, VCC (To the input of the opto-isolator, next to the IN pins) should be connected to the 3.3V device's +3.3V supply.

See the picture below: A is an electromagnet, B armature, C spring, D moving contact, and E fixed contacts. There are two fixed contacts, a normally closed one and a normally open one. When the coil is not energized, the normally open contact is the one that is off, while the normally closed one is the other that is on.

The 2-Channel Relay Module includes the following features:

TABLE 4.1:2 Channel Relay Module Features

Number of Relays	2
Control Signal	TTL Level
Rated Load	7A/240VAC 10A/125VAC 10A/28VDC
Contact Action Time	10ms/5ms
Interface Board	5V 2-Channel Relay interface board, and each one need 15-20mA Driver Current.
Equipment	<ul style="list-style-type: none"> Equipped with high-current relay, AC250V 10A; DC30V 10A Indication LED's for Relay output status.
Supported Microcontrollers	Standard interface that can be controlled directly by microcontroller (Arduino, 8051, AVR, PIC, DSP, ARM, ARM, MSP430, TTL logic)

Supply voltage to the coil and some currents will pass through the coil thus generating the electromagnetic effect. So the armature overcomes the tension of the spring and is attracted to the core, thus closing the moving contact of the armature and the normally open (NO) contact or you may say releasing the former and the normally closed (NC) contact. After the coil is de-energized, the electromagnetic force disappears and the armature moves back to the original position, releasing the moving contact and normally closed contact. The closing and releasing of the contacts results in power on and off of the circuit.

When a low level is supplied to signal terminal of the 2-channel relay, the LED at the output terminal will light up. Otherwise, it will turn off. If a periodic high and low level is supplied to the signal terminal, you can see the LED will cycle between on and off.

After the coil is de-energized, the electromagnetic force disappears and the armature moves back to the original position, releasing the moving contact and normally closed contact. The closing and releasing of the contacts results in power on and off of the circuit.

5. INTELLIGENT GSM DEVICE FOR AUTOMATION AND HOME AUTOMATION IMPLEMENTATION

In these days, the GSM mobile terminal has become one of the items that are constantly with us. Just like our wallet/purse, keys or watch, the GSM mobile terminal provides us a communication channel that enables us to communicate with the world. The requirement for a person to be reachable or to call anyone at any time is very appealing.

In this paper, as the name says paper is based on GSM network technology for transmission of SMS from sender to receiver. SMS sending and receiving is used for ubiquitous access of appliances and allowing breach control at home. The system proposes two sub-systems. Appliance control subsystem enables the user to control home appliances remotely and the security alert subsystem gives the automatic security monitoring.

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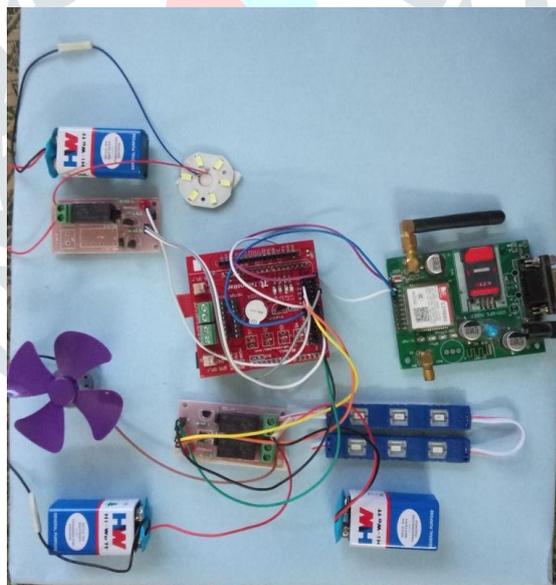


FIG 4.3 .Intelligent GSM Device for Automation and Home Automation implementation

6. APPLICATIONS

- Lightning control : Smart lightning allows you to control wall switches , blinds and lamp . Also you are able to schedules the time light should turn on and off and decides level of light should be emitted .
- HVAC regulation : Heating and cooling our homes consumes an average of 50% of energy costs yearly ,making daily HVAC regulation progressively. With automated HVAC you are able to reduce heat when room is unoccupied , and increases or decreases it at specific time based on your schedule .
- Lawn Irrigation System : The grass is always greener
- Security system : There is great deal of scrutiny regarding the level of trust in controlling your home security system via a mobile device , but it begs earnest exploration when weighing the potential benefits .
- Home automation
- Office automation
- In public distribution systems

- It is used to improve security of our home and office
- Remote operations in industries
- Energy conservation

7.CONCLUSION

It can be concluded that HOME AUTOMATION SYSTEM USING ARDUINO was a success. This system consists of an Arduino-Uno board, a GSM Module, an Android phone, power sockets, home appliances. It is user friendly and it is cost effective. Also it can be concluded that the objectives of this paper has been successfully met and they are as Constructed a wireless home automation system controlled by a GSM phone or SMART phone specifically an OLD GSM device or ANDRIOD device. Designed and implement cost effective home automation system yet an efficient one. Designed a user friendly and a safe system to control home appliances especially aimed to aid the elders and handicapped.

8.FUTURE SCOPE

All the technique may be updated to the new one such as WiFi (wireless-fidelity) is converted into the LiFi (LightFidelity). It takes a little bit time to change the WiFi into LiFi. LiFi work with presence of light so in night time the speed may be affected. Light from LED can be used for internet this will overcome the above problem. We can control the camera, PDA, and other appliances using it. Camera module can be used for security purpose also which store the images in cloud.

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3.1 Population and Sample

KSE-100 index is an index of 100 companies selected from 580 companies on the basis of sector leading and market capitalization. It represents almost 80% weight of the total market capitalization of KSE. It reflects different sector company's performance and productivity. It is the performance indicator or benchmark of all listed companies of KSE. So it can be regarded as universe of the study. Non-financial firms listed at KSE-100 Index (74 companies according to the page of KSE visited on 20.5.2015) are treated as universe of the study and the study have selected sample from these companies.

The study comprised of non-financial companies listed at KSE-100 Index and 30 actively traded companies are selected on the bases of market capitalization. And 2015 is taken as base year for KSE-100 index.

3.2 Data and Sources of Data

For this study secondary data has been collected. From the website of KSE the monthly stock prices for the sample firms are obtained from Jan 2010 to Dec 2014. And from the website of SBP the data for the macroeconomic variables are collected for the period of five years. The time series monthly data is collected on stock prices for sample firms and relative macroeconomic variables for the period of 5 years. The data collection period is ranging from January 2010 to Dec 2014. Monthly prices of KSE - 100 Index is taken from yahoo finance.

3.3 Theoretical framework

Variables of the study contains dependent and independent variable. The study used pre-specified method for the selection of variables. The study used the Stock returns are as dependent variable. From the share price of the firm the Stock returns are calculated. Rate of a stock salable at stock market is known as stock price.

Systematic risk is the only independent variable for the CAPM and inflation, interest rate, oil prices and exchange rate are the independent variables for APT model.

Consumer Price Index (CPI) is used as a proxy in this study for inflation rate. CPI is a wide basic measure to compute usual variation in prices of goods and services throughout a particular time period. It is assumed that arise in inflation is inversely associated to security prices because Inflation is at last turned into nominal interest rate and change in nominal interest rates caused change in discount rate so discount rate increase due to increase in inflation rate and increase in discount rate leads to decrease the cash flow's present value (Jecheche, 2010). The purchasing power of money decreased due to inflation, and due to which the investors demand high rate of return, and the prices decreased with increase in required rate of return (Iqbal et al, 2010).

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I. RESEARCH METHODOLOGY

The methodology section outline the plan and method that how the study is conducted. This includes Universe of the study, sample of the study, Data and Sources of Data, study’s variables and analytical framework. The details are as follows;

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Consumer Price Index (CPI) is used as a proxy in this study for inflation rate. CPI is a wide basic measure to compute usual variation in prices of goods and services throughout a particular time period. It is assumed that arise in inflation is inversely associated to security prices because Inflation is at last turned into nominal interest rate and change in nominal interest rates caused change in discount rate so discount rate increase due to increase in inflation rate and increase in discount rate leads to decrease the cash flow’s present value (Jecheche, 2010). The purchasing power of money decreased due to inflation, and due to which the investors demand high rate of return, and the prices decreased with increase in required rate of return (Iqbal et al, 2010).

Exchange rate is a rate at which one currency exchanged with another currency. Nominal effective exchange rate (Pak Rupee/U.S.D) is taken in this study. This is assumed that decrease in the home currency is inversely associated to share prices (Jecheche, 2010). Pan et al. (2007) studied exchange rate and its dynamic relationship with share prices in seven East Asian Countries and concluded that relationship of exchange rate and share prices varies across economies of different countries. So there may be both possibility of either exchange rate directly or inversely related with stock prices. Oil prices are positively related with share prices if oil prices increase stock prices also increase (Iqbal et al, 2012). Atallah (2001) suggested that oil prices cause positive change in the movement of stock prices. The oil price has no significant effect on stock prices (Dash & Rishika, 2011). Six month T-bills rate is used as proxy of interest rate. As investors are very sensitive about profit and where the signals turn into red they definitely sell the shares. And this sensitivity of the investors towards profit effects the relationship of the stock prices and interest rate, so the more volatility will be there in the market if the behaviors of the investors are more sensitive. Plethora (2002) has tested interest rate sensitivity to stock market returns, and concluded an inverse relationship between interest rate and stock returns. Nguyen (2010) studies Thailand market and found that Interest rate has an inverse relationship with stock prices.

KSE-100 index is used as proxy of market risk. KSE-100 index contains top 100 firms which are selected on the bases of their market capitalization. Beta is the measure of systematic risk and has a linear relationship with return (Horn, 1993). High risk is associated with high return (Basu, 1977, Reiganum, 1981 and Gibbons, 1982). Fama and MacBeth (1973) suggested the existence of a significant linear positive relation between realized return and systematic risk as measured by β . But on the other side some empirical results showed that high risk is not associated with high return (Michailidis et al. 2006, Hanif, 2009). Mollah and Jamil (2003) suggested that risk-return relationship is not linear perhaps due to high volatility.

3.4 Statistical tools and econometric models

This section elaborates the proper statistical/econometric/financial models which are being used to forward the study from data towards inferences. The detail of methodology is given as follows.

3.4.1 Descriptive Statistics

Descriptive Statics has been used to find the maximum, minimum, standard deviation, mean and normally distribution of the data of all the variables of the study. Normal distribution of data shows the sensitivity of the variables towards the periodic changes and speculation. When the data is not normally distributed it means that the data is sensitive towards periodic changes and speculations which create the chances of arbitrage and the investors have the chance to earn above the normal profit. But the assumption of the APT is that there should not be arbitrage in the market and the investors can earn only normal profit. Jarque bera test is used to test the normality of data.

3.4.2 Fama-McBeth two pass regression

After the test statistics the methodology is following the next step in order to test the asset pricing models. When testing asset pricing models related to risk premium on asset to their betas, the primary question of interest is whether the beta risk of particular factor is priced. Fama and McBeth(1973)develop a two pass methodology in which the beta of each asset with respect to a factor is estimated in a first pass time series regression and estimated betas are then used in second pass cross sectional regression to estimate the risk premium of the factor. According to Blum (1968) testing two-parameter models immediately presents an unavoidable errors-in-the variables problem. It is important to note that portfolios (rather than individual assets) are used for the reason of making the analysis statistically feasible. Fama McBeth regression is used to attenuate the problem of errors-in-variables (EIV) for two parameter models (Campbell, Lo and MacKinlay, 1997). If the errors are in the β (beta) of individual security are not perfectly positively correlated, the β of portfolios can be much more precise estimates of the true β (Blum, 1968).

The study follow Fama and McBeth two pass regression to test these asset pricing models. The Durbin Watson is used to check serial correlation and measures the linear association between adjacent residuals from a regression model. If there is no serial correlation, the DW statistic will be around 2. The DW statistic will fall if there is positive serial correlation (in worst case, it will be near zero). If there is a negative correlation, the statistic will lie somewhere between 2 and 4. Usually the limit for non-serial correlation is considered to be DW is from 1.8 to 2.2. A very strong positive serial correlation is considered at DW lower than 1.5 (Richardson and smith, 1993).

According to Richardson and smith(1993) to make the model more effective and efficient the selection criteria for the shares in the period are: Shares with no missing values in the period, Shares with adjusted $R^2 < 0$ or F significant (p-value) > 0.05 of the first pass regression of the excess returns on the market risk premium are excluded. And Shares are grouped by alphabetic order into group of 30 individual securities (Roll and Ross, 1980).

3.4.2.1 Model for CAPM

In first pass the linear regression is used to estimate beta which is the systematic risk.

$$R_i - R_f = (R_m - R_f)\beta \quad (3.1)$$

Where R_i is Monthly return of thesecurity, R_f is Monthly risk free rate, R_m is Monthly return of market and β is systematic risk (market risk).

The excess returns $R_i - R_f$ of each security is estimated from a time series share prices of KSE-100 index listed shares for each period under consideration. And for the same period the market Premium $R_m - R_f$ also estimated. After that regress the excess returns $R_i - R_f$ on the market premium $R_m - R_f$ to find the beta coefficient (systematic risk).

Then a cross sectional regression or second pass regression is used on average excess returns of the shares and estimated betas.

$$\hat{R}_i = \gamma_0 + \gamma_1\beta_i + \epsilon \quad (3.2)$$

Where $\lambda_0 =$ intercept, \hat{R}_i is average excess returns of security i , β_i is estimated be coefficient of security i and ϵ is error term.

3.4.2.2 Model for APT

In first pass the betas coefficients are computed by using regression.

$$R_i - R_f = \beta_i f_1 + \beta_{i2} f_2 + \beta_{i3} f_3 + \beta_{i4} f_4 + \epsilon \quad (3.3)$$

Where R_i is the monthly return of stock i , R_f is risk free rate, β_i is the sensitivity of stock i with factors and ϵ is the error term.

Then a cross sectional regression or second pass regression is used on average excess returns of the shares on the factor scores.

$$\hat{R} = \gamma_0 + \gamma_1\beta_1 + \gamma_2\beta_2 + \gamma_3\beta_3 + \gamma_4\beta_4 + \epsilon_i \quad (3.4)$$

Where \hat{R} is average monthly excess return of stock i , $\lambda =$ risk premium, β_1 to β_4 are the factors scores and ϵ_i is the error term.

3.4.3 Comparison of the Models

The next step of the study is to compare these competing models to evaluate that which one of these models is more supported by data. This study follows the methods used by Chen (1983), the Davidson and Mackinnon equation (1981) and the posterior odds ratio (Zellner, 1979) for comparison of these Models.

3.4.3.1 Davidson and MacKinnon Equation

CAPM is considered the particular or strictly case of APT. These two models are non-nested because by imposing a set of linear restrictions on the parameters the APT cannot be reduced to CAPM. In other words the models do not have any common variable. Davidson and MacKinnon (1981) suggested the method to compare non-nested models. The study used the Davidson and MacKinnon equation (1981) to compare CAPM and APT.

This equation is as follows;

$$R_i = \alpha R_{APT} + (1 - \alpha)R_{CAPM} + e_i \quad (3.5)$$

Where R_i = the average monthly excess returns of the stock i , R_{APT} = expected excess returns estimated by APT, R_{CAPM} = expected excess returns estimated by CAPM and α measure the effectiveness of the models. The APT is the accurate model to forecast the returns of the stocks as compare to CAPM if α is close to 1.

3.4.3.2 Posterior Odds Ratio

A standard assumption in theoretical and empirical research in finance is that relevant variables (e.g stock returns) have multivariate normal distributions (Richardson and Smith, 1993). Given the assumption that the residuals of the cross-sectional regression of the CAPM and the APT satisfy the IID (Independently and identically distribution) multivariate normal assumption (Campbell, Lo and MacKinlay, 1997), it is possible to calculate the posterior odds ratio between the two models. In general the posterior odds ratio is a more formal technique as compare to DM equation and has sounder theoretical grounds (Aggelidis and Maditinos, 2006).

The second comparison is done using posterior odd ratio. The formula for posterior odds is given by Zellner (1979) in favor of model 0 over model 1.

The formula has the following form;

$$R = [ESS_0/ESS_1]^{N/2} N^{K_0-K_1/2} \quad (3.6)$$

Where ESS_0 is error sum of squares of APT, ESS_1 is error sum of squares of CAPM, N is number of observations, K_0 is number of independent variables of the APT and K_1 is number of independent variables of the CAPM. As according to the ratio when;

$R > 1$ means CAPM is more strongly supported by data under consideration than APT.

$R < 1$ means APT is more strongly supported by data under consideration than CAPM.

IV. RESULTS AND DISCUSSION

4.1 Results of Descriptive Statics of Study Variables

Table 4.1: Descriptive Statics

Variable	Minimum	Maximum	Mean	Std. Deviation	Jarque-Bera test	Sig
KSE-100 Index	-0.11	0.14	0.020	0.047	5.558	0.062
Inflation	-0.01	0.02	0.007	0.008	1.345	0.510
Exchange rate	-0.07	0.04	0.003	0.013	1.517	0.467
Oil Prices	-0.24	0.11	0.041	0.060	2.474	0.290
Interest rate	-0.13	0.05	0.047	0.029	1.745	0.418

Table 4.1 displayed mean, standard deviation, maximum minimum and jarque-bera test and its p value of the macroeconomic variables of the study. The descriptive statistics indicated that the mean values of variables (index, INF, EX, OilP and INT) were 0.020, 0.007, 0.003, 0.041 and 0.047 respectively. The maximum values of the variables between the study periods were 0.14, 0.02, 0.04, 0.41, 0.11 and 0.05 for the KSE- 100 Index, inflation, exchange rate, oil prices and interest rate.

The standard deviations for each variable indicated that data were widely spread around their respective means.

Column 6 in table 4.1 shows jarque bera test which is used to check the normality of data. The hypotheses of the normal distribution are given;

H_0 : The data is normally distributed.

H_1 : The data is not normally distributed.

Table 4.1 shows that at 5 % level of confidence, the null hypothesis of normality cannot be rejected. KSE-100 index and macroeconomic variables inflation, exchange rate, oil prices and interest rate are normally distributed.

The descriptive statistics from Table 4.1 showed that the values were normally distributed about their mean and variance. This indicated that aggregate stock prices on the KSE and the macroeconomic factors, inflation rate, oil prices, exchange rate, and interest rate are all not too much sensitive to periodic changes and speculation. To interpret, this study found that an individual investor could not earn higher rate of profit from the KSE. Additionally, individual investors and corporations could not earn higher profits and interest rates from the economy and foreign companies could not earn considerably higher returns in terms of exchange rate. The investor could only earn a normal profit from KSE.

Figures and Tables

Place figures and tables at the top and bottom of columns. Avoid placing them in the middle of columns. Large figures and tables may span across both columns. Figure captions should be below the figures; table captions should appear above the tables. Insert figures and tables after they are recited in the text. Use the abbreviation “**Fig.1**” in the text, and “**Figure 1**” at the beginning of a sentence.

Use 10 **point Times New Roman** for figure labels. Use words rather than symbols or abbreviations when writing figure-axis labels to avoid confusing the reader. As an example, write the quantity “Magnetization”, or “Magnetization, M”, not just “M”.

Table 1 Table Type Styles

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IV. ACKNOWLEDGMENT

The preferred spelling of the word “acknowledgment” in America is without an “e” after the “g”. Avoid the stilted expression, “One of us (R.B.G.) thanks...” Instead, try “R.B.G. thanks”. Put applicable sponsor acknowledgments here; **DONOT** place them on the first page of your paper or as a footnote.

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