Essays on Stock Market Integration

- On Stock Market Efficiency, Price Jumps and Stock Market Correlations

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Akademisk avhandling


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Abstract
This thesis consists of four self-contained papers related to the change of market structure and the quality of equity market.

In Paper [I] we found, by using of a Flexible Dynamic Component Correlations (FDCC) model, that the creation of a common cross-border stock trading platform has increased the long-run trends in conditional correlations between foreign and domestic stock market returns.

In Paper [II] we study whether the creation of a uniform Nordic and Baltic stock trading platform has affected weak-form information efficiency. The results indicate that the stock market consolidations have had a positive effect on the information efficiency and turnover for an average firm. The merger effects are, however, asymmetrically distributed in the sense that relatively large (small) firms located on relatively large (small) markets experience an improved (reduced) information efficiency and turnover. Although the results indicate that changes in the level of investor attention (measured by turnover) may explain part of the changes in information efficiency, they also lend support to the hypothesis that merger effects may partially be driven by changes in the composition of informed versus uninformed investors following a stock.

Paper [III] analyzes whether the measured level of trust in different countries can explain bilateral stock market correlations. One finding is that generalized trust among nations is a robust predictor for stock market correlations. Another is that the trust effect is larger for countries which are close to each other. This indicates that distance mitigates the trust effect. Finally, we confirm the effect of trust upon stock market correlations, by using particular trust data (bilateral trust between country A and country B) as an alternative measurement of trust.

In Paper [IV] we present the impact of the stock market mergers that took place in the Nordic countries during 2000 – 2007 on the probabilities for stock price jumps, i.e. for relatively extreme price movements. The main finding is that stock market mergers, on average, reduce the likelihood of observing stock price jumps. The effects are asymmetric in the sense that the probability of sudden price jumps is reduced for large and medium size firms whereas the effect is ambiguous for small size firms. The results also indicate that the market risk has been reduced after the stock market consolidations took place.

Keywords
Time-varying return predictability, Tests for jumps, International financial markets, Market structure, Common trading platform, Integration, Time-varying correlation, C-GARCH, Trust, Portfolio Diversification, Stock Market Participation