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Emerging Markets Queries in Finance and Business

The Impact of Euro Area Macroeconomic Announcements on CIVETS Stock Markets

Elena Fedorova[a*], Laura Wallenius[a], Mikael Collan[a]

[a] *School of Business, Lappeenranta University of Technology, Skinnarilankatu 34, Lappeenranta 53850, Finland*

Abstract

This paper studies theimpact of euro area macroeconomic announcements on CIVETS (Colombia, Indonesia, Vietnam, Egypt, Turkey, and South Africa) stock markets. A link between euro area macroeconomic announcements and CIVETS stock markets is found. The data used is from between 2007 and 2012.Euro area macroeconomic news are shown to affect CIVETS stock market volatility and in some instances the stock returns. Evidence on the impact of overall European macroeconomic news on stock market volatility is found for Colombia, Vietnam, Egypt, and Turkey. European announcements about GDP, retail sales, and unemployment have a significant effect on the stock returns. According to our results, CIVETS stock markets seem to exhibit a negative relationship between market returns and volatility: negative news have a leverage effect for the most of CIVETS stock markets, as greater volatility is generated by negative than by positive shocks. The results may be applied for asset pricing and portfolio selection and the assessment of investment decisions with respect to macroeconomic news releases.

*Keywords:*macroeconomic announcements, stock market integration, spillovers, emerging markets, CIVETS

1. Introduction

Many emerging countries have become major determinants of global prosperity, contributing from one-quarter to one-half of the global growth (Johnson, 2008). Emerging markets have been able to sustain their growth despite the financial turbulence of the recent years, likely due to the fact that they are not yet fully

* * Corresponding author. Tel.: +358-29-446-3246; mob: +358-50-322-6538.
E-mail address: elena.fedorova@lut.fi.

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integrated in terms of financial flows to the developed economies. Furthermore, the importance of so-called south-south trade has increased and helped emerging markets sustain growth. Due to growing market integration among the developed economies and the negative spillovers of the global financial crisis and the euro crisis between the developed economies, emerging and frontier economies have received attention from the international investment community as the source for possible higher returns and diversification opportunities. CIVETS (Colombia, Indonesia, Vietnam, Egypt, Turkey, and South Africa) countries are a part of these emerging economies that have in the recent years opened their markets to foreign investments and international trade, and thus are an interesting area for study of spill-over effects. It can be expected that their exposure to external shocks from global markets has increased in the wake of their internationalization.

The purpose of this research is to investigate if (and to what extent) CIVETS stock markets are integrated with the euro area (EA) as measured by the impact of scheduled EA macroeconomic news announcements; in fact,this research is the first study on impact of EA macroeconomic news announcements on CIVETS stock markets. To the best of the authors' knowledge, the research by Korkmaz et al., 2012 and Yi et al.,2013 are the only other studies that have studied CIVETS as a group with regards to spill-over effects.

Macroeconomic announcements provide insight into national or regional economic trends for economists and market participants around the world and may affect financial markets. With these announcements financial institutions and investors try to anticipate the expected asset returns. In this research, eight commonly used scheduled macroeconomic news announcements (eight indicators) from EA are introduced and applied in the empirical part to study their impact on six CIVETS stock markets' returns and volatilities. Daily market data from CIVETS has been collected for the research period from 2007 to 2012. The econometric model used in this research is Exponential Generalized Autoregressive Conditional Heteroscedasticity (EGARCH).

EA is among the main trading partners and sources of foreign direct investment into CIVETS. The starting hypothesis is that stock returns and/or volatilities react, to some extent, to the incoming information from EA. It is also expected that due to the heterogeneity of CIVETS markets(differences in the size of the market, industrial structures, political and economic ties, and dependence on international trade) there are differences in the impacts between countries.

The remainder of this paper is organized as follows. The following section presents the theoretical background of studying the effects of macroeconomic announcements on local stock markets. Section 3 provides descriptive statistics for the stock markets and description of macroeconomic announcements that are examined in this study. Model specification applied to test impact of EA macroeconomic announcements is introduced in Section 4. Section 5presents the results from the model estimation of this study and section6 concludes the paper and provides suggestions for future research.

2. Background

Previous research regarding the effects of macroeconomic news announcements on stock returns is vast, but has mainly concentrated on the relationships between developed economies. Only recently studies that have examined the effects of macroeconomic news announcements on emerging economies have arisen. Andersen et al. (2007) examined the interactions among U.S., German, and British stock, bond, and foreign exchange markets with respect to the U.S. macroeconomic news announcements. They found that stock, bond, and exchange rate dynamics are linked to macroeconomic fundamentals. Bollerslev et al., 2000 found that regularly scheduled macroeconomic news announcements are an important source of volatility at the intraday level in the U.S. Treasury bond market. Additionally, the authors found that the largest returns in the U.S. Treasury bond market are linked to the release of macroeconomic news announcements. Nofsinger and Prucyk, 2003 found that bad news creates high volatility and high volume, whereas good news elicits lower volume and is not associated with higher volatility.