

Accepted Manuscript

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PII: S0378-4371(17)30073-0

DOI: <http://dx.doi.org/10.1016/j.physa.2017.01.063>

Reference: PHYSA 17956

To appear in: *Physica A*

Received date: 30 November 2016

Please cite this article as: N.A. Rahahleh, M. Ishaq Bhatti, I. Adeinat, Tail dependence and information flow: Evidence from international equity markets, *Physica A* (2017), <http://dx.doi.org/10.1016/j.physa.2017.01.063>

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Tail Dependence and Information Flow: Evidence from International Equity Markets

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Abstract

Bhatti and Nguyen (2012) used the copula approach to measure the tail dependence between a number of international markets. They observed that some country pairs exhibit only left-tail dependence whereas others show only right-tail. However, the flow of information from uni-dimensional (one-tail) to bi-dimensional (two-tails) between various markets was not accounted for. In this study, we address the flow of information of this nature by using the dynamic conditional correlation (DCC-GARCH) model. More specifically, we use various versions of the DCC models to explain the nexus between the information flow of international equity and to explain the stochastic forward vs. backward dynamics of financial markets based on data for a 15-year period comprising 3,782 observations. We observed that the information flow between the US and Hong Kong markets and between the US and Australian markets are bi-directional. We also observed that the DCC model captures a wider co-movement structure and interconnectedness compared to the symmetric Joe-Clayton copula.

Keywords: DCC models, Copula, Equity market, Left-tail dependence, Spillover effect

JEL classification: G15, F36, C32, C58

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