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# Investor attention to the Eurozone crisis and herding effects in national bank stock indexes <sup>☆</sup>



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### ABSTRACT

In this study, we investigate the relation between investor attention to the Eurozone crisis and herding effects in national bank stock indexes across Europe. We especially focus on two different groups of European countries: non-EMU member countries and EMU member countries. Our results suggest that an increased investor attention to the Eurozone crisis decreased herding effects in the EMU region in the following week, but the effect was temporary as the effect became the opposite with a two-week lag. Herding effects in the EMU region affected herding effects in the non-EMU region, but not vice versa.

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## 1. Introduction

The Eurozone crisis, which started in 2010, led to great uncertainty and doubt about the health of many European economies and their banking sectors. During the crisis, it became popular among practitioners and market commentators to pay more attention to the banking sector in Europe, which was involved heavily in the crisis due to the risk exposures of the banks. However, the effect of increased investor attention in these situations is still an unexplored research direction.

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In this study, we investigate the relation between investors' crisis attention and herding effects in national bank stock indexes across Europe during the period from September 26, 2008 to January 31, 2014 with a particular focus on the differences between non-EMU member and EMU-member European countries. We examine whether herding effects in national bank stock indexes, measured as the cross-sectional dispersion of returns, across Europe changed with investor attention to the Eurozone crisis. If investor attention to the crisis were to increase herding effects, the effect would mean less diversification possibilities for investors.

We follow a similar approach to the studies by [Da et al. \(2011\)](#), and measure investor attention to the European debt crisis by using the Google Search Volume Index (GSVI) of "euro crisis". The study shows evidence on how the GSVI for different search terms contains predictive information for future stock returns. [Smith \(2012\)](#), [Aouadi et al. \(2013\)](#), and [Andrei and Hasler \(2015\)](#), in turn, present evidence that Google search volumes can be used to explain volatility in stock and foreign currency markets. We expect that investor attention to the Eurozone crisis decreases herding effects because increased attention helps investors to process information, which supports efficient price discovery. This presumption is supported by [Vozlyublennai \(2014\)](#), who shows evidence by using the GSVI that investor attention improves market efficiency. Additionally, [Peng et al. \(2007\)](#) present evidence that stock co-movement decreases in the five days following macroeconomic shocks.

In relation to previous studies, we aim to delve into the role of investor attention to the Eurozone crisis as a determinant of herding effects, while the evidence on herding effects in a crisis is still mixed. [Philippas et al. \(2013\)](#) find evidence on herding effects in the US REIT market that the global financial crisis did not increase herding effects in the US REIT market. [Asma et al. \(2014\)](#), in turn, present evidence for significant herding effects in the stock markets of various European countries during the global financial crisis and the Eurozone crisis. The results of our study suggest that investor attention to the Eurozone crisis had a significant impact on herding effects in the EMU region. Herding effects in the EMU region affected herding effects in the non-EMU region, but not vice versa.

The remainder of the paper is organized as follows: In Section 2, we review the relevant literature on the behavior of European bank stock indexes. Section 3 is for the presentation of the data and methods used in our study. In Section 4, we present our results, which are followed by our conclusions in Section 5.

## 2. Related research on European stock markets

The question of whether European bank stock indexes exhibit herding effects is also an issue of diversification benefits because more herding means fewer benefits from diversification. [Flavin \(2004\)](#) presents evidence that, within Europe, the importance of country diversification has transformed into the importance of industry diversification. In line with this finding, the results of [Kim et al. \(2005\)](#) suggest that stock market integration has increased as a result of the euro's introduction. [Alexandrou et al. \(2011\)](#) investigate the integration process of the banking industry in Europe by using four different bank stock groups in their analyses: (1) euro-adopters, (2) non-euro-adopters, (3) new EMU members, and (4) non-EMU members. The authors present evidence indicating that the introductions of the euro and the enlargement of the EU in May 2004 have contributed to the integration process.

However, investors are still likely to benefit from diversification between European countries, although the benefits have decreased. For one thing, [Mylonidis and Kollias \(2010\)](#) present evidence that even though four major European stock markets have converged after the introduction of the euro, the convergence of the different markets is not complete. For another, [Sminou \(2011\)](#) examines the impact of the introduction of the euro by investigating the country portfolio diversification of stocks. His results suggest that diversification benefits still exist after the adoption of the euro and that the diversification benefits between non-EMU members appear to be stronger after the introduction of the euro.

While financial market integration in the EMU region has shown to have increased, the recent financial crisis may also have affected integration. The evidence of [Bartman and Bodnar \(2009\)](#) and [Yang et al. \(2002\)](#) indicates that markets are more integrated during a financial turmoil and bear markets than during growth periods. Thus, the Eurozone crisis should have affected the behavior of

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