

International Equity Markets

Chapter Eight

8

Chapter Objective:

This chapter discusses both the primary and secondary equity markets throughout the world.

Chapter Outline

- A Statistical Perspective
- Market Structure, Trading Practices, and Costs
- International Equity Market Benchmarks
- World Equity Market Benchmark Shares
- Trading in International Equities
- Factors Affecting International Equity Returns

A Statistical Perspective

- Market Capitalization of Developed Countries
- Market Capitalization of Developing Countries
- Measures of Liquidity
- Measures of Market Concentration

Market Capitalization of Developed Countries

- Almost 90% of the total market capitalization of the world's equity markets is accounted for by the market capitalization of the developed world.

Market Capitalization of Developing Countries

- The other 10% is accounted for by the market capitalization of developing countries in “emerging markets”.
 - Latin America
 - Asia
 - Eastern Europe
 - Mideast/Africa
- Recently the growth rates in these emerging markets have been strong, but with more volatility than we have here at home.

Measures of Liquidity

- The equity markets of the developed world tend to be much more liquid than emerging markets.
 - Liquidity refers to how quickly an asset can be sold without a major price concession.
- So, while investments in emerging markets may be profitable, the focus should be on the long term.

Measures of Market Concentration

- Emerging Markets tend to be much more concentrated than our markets.
 - Concentrated in relatively few companies.
- That is, a few issues account for a much larger percentage of the overall market capitalization in emerging markets than in the equity markets of the developed world.

Market Structure, Trading Practices, and Costs

- Primary Markets
 - Shares offered for sale directly from the issuing company.
- Secondary Markets
 - Provide market participants with marketability and share valuation.

Market Structure, Trading Practices, and Costs

- Market Order
 - An order to your broker to buy or sell share immediately at the market price.
- Limit Order
 - An order to your broker to buy or sell at the at a price you want, when and if he can.
- If immediate execution is more important than the price, use a market order.

Market Structure, Trading Practices, and Costs

- Dealer Market
 - The stock is sold by dealers, who stand ready to buy and sell the security for their own account.
 - In the U.S., the OTC market is a dealer market.
- Auction Market
 - Organized exchanges have specialists who match buy and sell orders. Buy and sell orders may get matched without the specialist buying and selling as a dealer.
- Automated Exchanges
 - Computers match buy and sell orders.

International Equity Market Benchmarks

- North America
- Europe
- Asia/Pacific Rim

North American Equity Market Benchmarks

<i>Name</i>	<i>Symbol</i>
<i>Dow Jones Industrial Average</i>	DJIA
<i>NASDAQ Combined Composite</i>	CCMP
<i>S&P 500</i>	SPX
<i>TSE 300</i>	TS300
<i>Mexico BOLSA Index</i>	MEXBOL

European Equity Market Benchmarks

<i>Name</i>	<i>Symbol</i>
<i>FT-SE 100</i>	UKX
<i>CAC 40</i>	CAC
<i>Frankfurt DAX Index</i>	DAX
<i>IBEX Index</i>	IBEX
<i>Milan MIB30</i>	MIB30
<i>BEL20 Index</i>	BEL20

Asia/ Pacific Rim Equity Market Benchmarks

<i>Name</i>	<i>Symbol</i>
<i>NIKKEI 225 Index</i>	NKY
<i>Hang Seng Index</i>	HSI
<i>Sing Straits Times Index</i>	STI
<i>ASX All Ordinaries Index</i>	AS300

World Equity Benchmark Shares

- World Equity Benchmark Shares (WEBS)
 - Country-specific baskets of stocks designed to replicate the country indexes of 14 countries.
 - WEBS are subject to U.S. SEC and IRS diversification requirements.
 - Low cost, convenient way for investors to hold diversified investments in several different countries.

Trading in International Equities

- Magnitude of International Equity Trading
- Cross-Listing of Shares
- Yankee Stock Offerings
- The European Stock Market
- American Depository Receipts

Magnitude of International Equity Trading

During the 1980s world capital markets began a trend toward greater global integration.

Diversification, reduced regulation, improvements in computer and communications technology, increased demand from MNCs for global issuance.

Cross-Listing of Shares

- *Cross-Listing* refers to a firm having its equity shares listed on one or more foreign exchanges.
- The number of firms doing this has exploded in recent years.

Advantages of Cross-Listing

- It expands the investor base for a firm.
- Establishes name recognition for the firm in new capital markets, paving the way for new issues.
- May offer marketing advantages.
- May mitigate possibility of hostile takeovers.

Yankee Stock Offerings

- The direct sale of new equity capital to U.S. public investors by foreign firms.
 - Privatization in South America and Eastern Europe
 - Equity sales by Mexican firms trying to cash in on NAFTA

The European Stock Market

- EASDAQ is a sort of a European NASDAQ that binds together national exchanges.
- UK, Germany, France, Switzerland, Austria, Italy, Belgium, Denmark, Portugal, Finland, Greece, Luxembourg, and the Netherlands.
- All trading is denominated in the euro.

American Depository Receipts

- Foreign stocks often trade on U.S. exchanges as ADRs.
- It is a receipt that represents the number of foreign shares that are deposited at a U.S. bank.
- The bank serves as a transfer agent for the ADRs

American Depository Receipts

- There are many advantages to trading ADRs as opposed to direct investment in the company's shares:
 - ADRs are denominated in U.S. dollars, trade on U.S. exchanges and can be bought through any broker.
 - Dividends are paid in U.S. dollars.
 - Most underlying stocks are bearer securities, the ADRs are registered.

Factors Affecting International Equity Returns

- Macroeconomic Factors
- Exchange Rates
- Industrial Structure

Macroeconomic Factors Affecting International Equity Returns

- The data do not support the notion that equity returns are strongly influenced by macro factors.
- That is correspondent with findings for U.S. equity markets.

Exchange Rates

- Exchange rate movements in a given country appear to reinforce the stock market movements within that country.
- One should be careful not to confuse correlation with causality.

Industrial Structure

- Studies examining the influence of industrial structure on foreign equity returns are inconclusive.

End Chapter Eight