

Report Type

Mid Term Award Report

Full Name

Dr. Jisok Kang, Research Associate

Your E-Mail Address

j.kang@jbs.cam.ac.uk

Faculty/Department

Cambridge Endowment for Research in Finance

Project Title

Does the Stock Market Benefit the Economy?

Project Start Date

Jan 01, 2015

Project End Date

Dec 31, 2018

Project Abstract

An effectively functioning stock market allocates capital efficiently and provides sufficient funds to emerging, productive firms, which in turn breeds competition and innovation, ultimately fueling economic growth. In this paper, we show that concentrated stock markets dominated by a small number of large firms are functionally inefficient. Using data from 47 countries during 1989–2013, we find that capital is allocated inefficiently in countries with concentrated stock markets, which results in sluggish IPO activity, innovation, and economic growth.

Activities and Achievement

The paper “Does the Stock Market benefit the Economy?” coauthored with Kee-Hong Bae, explores the role of stock market functionality on economic growth. This topic has enormous implications for policymakers, particularly in developing economies with plans to develop stock markets. However, there is currently not enough evidence to support the positive role of the stock market on the economy. In this paper, we first develop a new (inverse) proxy for stock market functionality, in contrast to other researchers who have used stock market size as a proxy for stock market development – an approach that has failed to establish a robust, causal relationship between stock market development and economic growth. Another innovation of our paper is to investigate the channels through which finance promotes growth, not just the causal relationship between these two. We show that an important role of the stock market is to provide necessary funds to new, small but innovative firms, rather than well-established large firms. This in turn breeds competition and innovation, which ultimately fuels economic growth. We are currently preparing a revision for the 2nd round at the Journal of Financial Economics.

Dissemination

The paper has been presented at numerous academic conferences such as Financial Management Association Annual Meeting in 2017. It has received a Revise and Resubmit recommendation from the Journal of Financial Economics and I am currently preparing a revision for the 2nd round at the Journal of Financial Economics with my co-author.

Outputs

The latest version of the paper is attached.

Major Difficulties and Any Other Issues

The paper is under revision for the 2nd round review at the Journal of Financial Economics.