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Research Papers

Titles: Cultural dispersion and stock liquidity

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Abstract:

Research Summary

This paper examines whether cultural dispersion of a multinational firm affects its stock trading in the market. The result shows that the stock liquidity negatively relates to the degree of cultural dispersion, suggesting it is costlier to trade stocks of culturally diverse firms. Among five measures of stock liquidity, Chae's (2005) turnover measure demonstrates the most consistent effect after addressing potential omitted variables and selection biases. A robustness test that extends our sample to include purely domestic firms confirms the main result of the negative effect of cultural dispersion. Furthermore, while the relation between cultural dispersion and stock liquidity may not be exactly linear, such a negative association overall holds. In addition, the influence of cultural dispersion on stock trading takes effects mainly through the agency and external information environment channels and is more pronounced for lower risk-taking multinationals.

Managerial Summary

This result has three practical implications for investment management. First, it is important to consider the internal cultural diversity when investing multinational firms. Second, the evaluation of firm liquidity goes beyond financial fundamentals or market mechanism. When a firm increase its degree of informational complexity and unfamiliarity, it tends to decrease its attractiveness to investors. Last but not least, when investing globally, cultural differences is an important consideration. Using stock liquidity as a research platform, this study suggests that the effect of cultural difference is indeed material.

Link : <https://doi.org/10.1002/gsj.1472>

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