Stock Prices of Domestic Banking Sector and External Shocks in East Asia

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Abstract

This paper examines the impact of fluctuation in foreign stock markets on the stock prices of domestic banks to explore if and how external shocks have affected the banking system in Korea, Malaysia, Singapore, and Thailand. These countries have consolidated the domestic banking system since the Asian crisis of 1997. Although some researchers insist that the shocks of global financial crisis in 2007–2009 on domestic banks in East Asia are small because of the improvement in the soundness of the banking system as a result of reforms, few previous articles have investigated how the banking sector of East Asian countries has been affected by external shocks. This study uses a multinominal logit model to estimate how changes in the stock price indices of the U.S. and Japan have an impact on the banking sector in Korea, Malaysia, Singapore, and Thailand. Regression employs the number of banks in a given country that experience a large shock on the same day (“coexceedances”) as shocks on the domestic banking sector. The regression result suggests that the fluctuation in the foreign stock market had a larger impact on the stock prices of the banking sector in the 2000s than in the 1990s before the Asian financial crisis. While the shocks of fall in foreign stock markets were significant in the 2000s before the global financial crisis, both shocks of rise and fall had an impact on the banking sector during the crisis of 2007–2009. The increasing international flow of capital and foreign assets and liabilities may have had a great influence in East Asia, while the domestic banking system has improved in the 2000s.

Keywords: Domestic banks; Stock prices; Foreign stock market; External influences; Asia
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