Predatory short-selling and covering around pre-announced deletions from index composition: Evidence from Nikkei 225 Index deletions

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Abstract

Focusing on pre-announced index deletions that induce liquidity needs on the part of index funds and using daily short selling data, we show that short sellers employ front-running strategies in which they sell stocks immediately after the announcements of deletions from index composition until the actual deletion day and buy back stocks thereafter. We find that, while short sellers can exploit profitable opportunities, their trading activities create temporary liquidity shortages and destabilize stock prices.

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