

International Equity Markets

Chapter 13

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EXHIBIT 13.1 (Excerpt) Market Capitalization (in billions of U.S.D.)

Exchange	2011	2012	2013	2014	2015
<i>Americas</i>					
Barbados Stock Exchange	NA	NA	NA	3	3
Bermuda Stock Exchange	1	1	1	2	2
BM&FBOVESPA	1,229	1,227	1,020	844	491
Bolsa de Comercio de Buenos Aires	44	34	53	60	56
Bolsa de Comercio de Santiago	270	313	265	233	190
Bolsa de Valores de Colombia	201	262	203	147	86
Bolsa de Valores de Lima	82	103	81	79	57
Bolsa de Valores de Panama	NA	NA	NA	14	13
Bolsa Mexicana de Valores	409	525	526	480	402
Bolsa Nacional de Valores	NA	NA	NA	3	2
Canadian Securities Exchange	NA	NA	NA	2	NA
Jamaica Stock Exchange	NA	NA	NA	3	6
Nasdaq-US	3,845	4,582	6,085	6,979	7,281
NYSE	11,796	14,086	17,950	19,351	17,787
TMX Group	1,912	2,059	2,114	2,094	1,592
Total Region	19,789	23,193	28,299	30,293	27,967

Market Capitalization

- At year-end 2015, total market capitalization of the 80 organized stock exchanges tracked by the World Federation of Exchanges stood at \$67,125 billion.

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Emerging Markets

- Standard & Poor's Emerging Markets Database classifies a stock market as “emerging” if it meets at least one of two general criteria:
 - It is located in a low- or middle-income economy as defined by the World Bank.
 - Its investable market capitalization is low relative to its most recent GNI figures.

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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 investor's focus should be on the long term.

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Measures of Liquidity

- One measure of liquidity for a stock market is the turnover ratio:

$$\text{turnover ratio} = \frac{\text{stock market transactions}}{\text{market capitalization}}$$
 - The higher the ratio, the more liquid the market.
 - Turnover ratios are relatively stable over time for most national stock exchanges.
 - Many national stock exchanges had relatively high turnover ratios, with over 40 percent of the exchanges in most years in excess of 30 percent turnover per month.

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EXHIBIT 13.2 (Excerpt)

Share Turnover Velocity (December)*

Exchange	2011 (in%)	2012 (in %)	2013 (in %)	2014 (in %)	2015 (in %)
<i>Americas</i>					
Barbados Stock Exchange	NA	NA	NA	0.2	30.8
Bermuda Stock Exchange	0.9	3.2	NA	2.5	0.7
BM&FBOVESPA	65.5	64.5	56.8	81.6	80.9
Bolsa de Comercio de Buenos Aires	3.1	5.3	5.2	4.8	5.2
Bolsa de Comercio de Santiago	21.3	16.8	17.4	10.5	8.1
Bolsa de Valores de Colombia	13.3	7.2	7.9	11.1	11.1
Bolsa de Valores de Lima	4.7	25.7	NA	5.5	1.6
Bolsa de Valores de Panama	NA	NA	4.0	2.0	1.4
Bolsa Mexicana de Valores	18.4	21.9	32.2	26.2	24.7
Jamaica Stock Exchange	NA	NA	NA	6.4	6.1
TMX Group	66.4	68.2	56.0	85.1	85.1

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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.

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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 a price you want, when and if he can.
- If immediate execution is more important than the price, use a market order.

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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.

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Market Consolidations And Mergers

- There are approximately 80 major national stock markets.
 - Western and Eastern Europe once had more than 20 national stock exchanges where at least 15 different languages were spoken.
 - It appears that over time a European stock exchange will eventually develop. However, a lack of common securities regulations, even among the countries of the European Union, is hindering this development.
- Today, stock markets around the world are under pressure from clients to combine or buy stakes in one another to trade shares of companies anywhere, at a faster pace.

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EXHIBIT 13.3 Characteristics of Major Equity Trading Systems

Equity Trading System	Market Characteristics		
	Public Orders	Order Flow	Example
Dealer	Trade with dealer	Continuous	NASDAQ/OTC
Agency	Agent assists with matching of public orders	Continuous or periodic	NYSE specialist system ^a (continuous) Old Paris Bourse (noncontinuous)
Fully automated	Electronic matching of public orders	Continuous	Toronto Stock Exchange

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Trading in International Equities

- Magnitude of international equity trading
- Cross-listing of shares
- Yankee stock offerings
- The European stock market
- American Depositary Receipts (ADRs)

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Magnitude of International Equity Trading

- During the 1980s world capital markets began a trend toward greater global integration.
- This trend was caused by diversification, reduced regulation, improvements in computer and communications technology, and an increased demand from MNCs for global issuance.

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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.

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Advantages of Cross-Listing

- It expands the investor base for a firm.
 - Very important advantage for firms from emerging market countries with limited capital markets.
- Establishes name recognition for the firm in new capital markets, paving the way for new issues.
- May offer marketing advantages.
- Cross-listing into developed markets with strict securities regulations and information disclosure may signal investors that improved corporate governance is forthcoming.
- May mitigate possibility of hostile takeovers.

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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” following implementation of NAFTA.

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EXHIBIT 13.4 (Excerpt) Total, Domestic, and Foreign Company Listings on Major National Stock Exchanges for 2015

Exchange	Total	Domestic	Foreign
<i>Americas</i>			
Barbados Stock Exchange	24	20	4
Bermuda Stock Exchange	67	14	53
BM&FBOVESPA	359	345	14
Bolsa de Comercio de Buenos Aires	99	93	6
Bolsa de Comercio de Santiago	310	223	87
Bolsa de Valores de Lima	310	212	98
Bolsa de Valores de Panama	31	30	1
Bolsa Mexicana de Valores	143	136	7
Bolsa Nacional de Valores	10	10	0
Jamaica Stock Exchange	60	59	1
Nasdaq - US	2,859	2,471	388
NYSE	2,424	1,910	514
TMX Group	3,559	3,501	58
Total Region	10,255	9,024	1,231

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American Depositary 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.

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Advantages of ADRs

- 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 and the ADRs are registered.
 - ADR trades clear in 3 business days whereas settlement practices for the underlying stock vary in foreign countries.

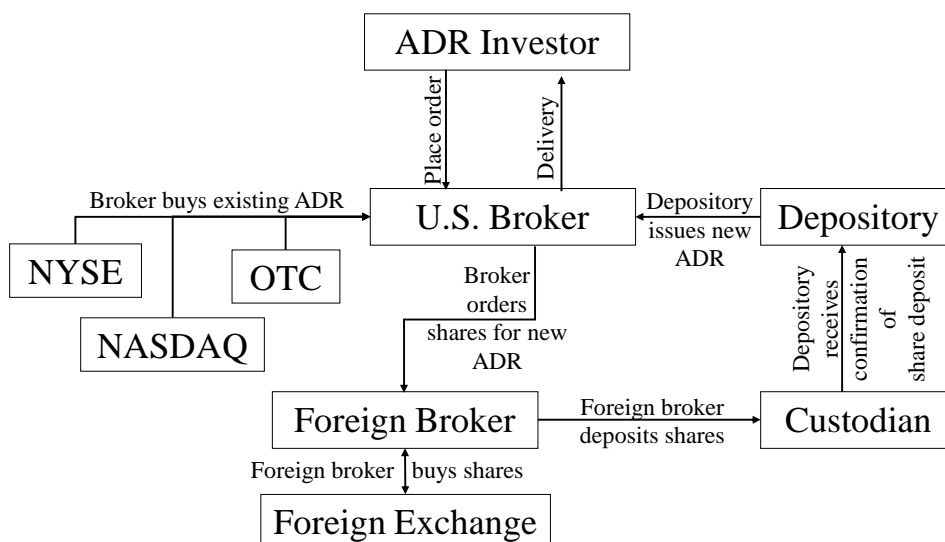
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Volvo ADR

- A good example of a familiar firm that trades in the U.S. as an ADR is Volvo AB, the Swedish car maker.
- Volvo trades in the U.S. on the NASDAQ under the ticker VOLVY.
 - The depository institution is JPMorgan ADR Group.
 - The custodian is a Swedish firm, S E Banken Custody.
- Of course, Volvo also trades on the Stockholm Stock Exchange under the ticker VOLVB.

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Mechanics of Issuance & Cancellation of ADRs



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EXHIBIT 13.6 Types of ADRs

	LEVEL I	LEVEL II	LEVEL III	RULE 144A
Description	Unlisted program in the U.S.	Listed on a U.S. exchange	Shares offered and listed on a U.S. exchange	Private placement to Qualified Institutional Buyers
Trading	OTC	NASDAQ, AMEX, NYSE	NASDAQ, AMEX, NYSE	U.S. private placement
SEC Registration	Form F-6	Form F-6	Forms F-1 and F-6	None
U.S. Reporting Requirements	Exempt under Rule 12g3-2(b)	Form 20-F*	Form 20-F*	Exempt under Rule 12g3-2(b)

*Financial statements must be partially reconciled to U.S. GAAP.

Level I: The most basic type of ADR program.

The Issuer is not seeking to raise new equity capital in the U.S. and/or cannot list on NASDAQ.

Level II: The Issuer is not seeking to raise new equity capital in the U.S. and ADRs can be listed on NASDAQ, AMEX, or NYSE.

Level III: The Issuer floats a public offering of new equity in the U.S. and lists the ADRs on NASDAQ, AMEX, or NYSE.

Rule 144A: This type of ADR program is a private placement of equity to Qualified Institutional Buyers (QIBs).

It can only be traded among QIBs.

Source: Excerpted from www.adr.com.

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Global Registered Shares

- The merger of Daimler Benz AG and Chrysler Corporation in November 1998 created DaimlerChrysler AG, a German firm. The merger simultaneously created a new type of equity share, called Global Registered Shares (GRSs).
- GRSs are traded globally, unlike ADRs, which are traded on foreign markets.
- The company was renamed Daimler AG in October 2007 when it spun off Chrysler. The primary exchanges for Daimler GRSs are the Frankfurt Stock Exchange and the NYSE; however, they are traded on a total of 20 exchanges worldwide.
- The shares are fully fungible—a GRS purchased on one exchange can be sold on another. They trade in both U.S. dollars and euro.

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Global Registered Shares

- The main advantage of GRSs over ADRs appears to be that all shareholders have equal status and direct voting rights.
- The main disadvantage of GRSs appears to be the greater expense in establishing the global registrar and clearing facility.
- GRSs have met with limited success; many companies that considered them opted instead for ADRs.
- Deutsche Bank, UBS, and NYSE Euronext also trade as GRSs.

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Empirical Findings on Cross-Listings and ADRs

- An internationally diversified portfolio of ADRs outperforms both a U.S. stock market and a world stock market benchmark on a risk-adjusted basis.
- For most stocks, the home-market price and the ADR price is within 20-85 basis points—thus limiting any arbitrage opportunities.

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EXHIBIT 13.8 Major National Stock Market Indexes

Country	Index	Country	Index	Country	Index
Argentina	Merval	Italy	FTSE MIB	Taiwan	Weighted Fr
Australia	All Ordinaries		FTSE Italia Mid Cap	Thailand	Bangkok SET
	S&P/ASX 200 Res		FTSE Italia All Sh	Turkey	BIST 100
	ATX	Japan	Nikkei 225	UAE	Abu Dhabi General Index
Austria	BEL 20		Tse		
Belgium	BEL Mid		S&P Topix 150	UK	FTSE 100
Brazil	Ibovespa	Jordan	2nd Section		FT 30
Canada	S&P/TSX Met & Min	Kenya	NSE 20		FTSE All Share
	S&P/TSX 60	Kuwait	KSE Market Index		FTSE uoMARK 100
	S&P/TSX Comp	Latvia	OMX Riga	USA	FTSE4Good UK
Chile	IGPA Gen	Lithuania	OMX Vilnius		S&P 500
China	Shanghai A	Luxembourg	IPC		FTSE NASDAQ 500
	Shanghai B	Malaysia	FTSE Bursa KLCI		NASDAQ Comp
	Shenzhen A	Mexico	IPC		NASDAQ 100
	Shenzhen B	Morocco	MASI		Russell 2000
	FTSE A200	Netherlands	AEX		NYSE Comp
	FTSE B35	New Zealand	AEX All Share		Wilshire 5000
Colombia	COLCAP	Nigeria	NZX 50		DI Industrial
Croatia	CROBEX	Norway	OSE All Share		DI Composite
Cyprus	CSE M&P Gen	Pakistan	KSE 100	Venezuela	DI Transport
Czech Republic	FX	Philippines	Musila Comp	Vietnam	DI Utilities
Denmark	OMX Copenhagen 20	Poland	Wig		IBC
Egypt	ECA 30	Portugal	PSI General		VNI
Estonia	OMX Tallinn	Romania	PSI 20		Stoxx 50
Finland	OMX Helsinki General	Russia	BET Index		Euro Stoxx 50
France	CAC 40		MICEX Comp.		DI Global Titans
	SBF 120	Saudi Arabia	TADAWUL All Share		Europe 1500 ID
Germany	M DAX		Index		FTSE Multiassets
	XETRA Dax	Singapore	FTSE Straits Times		FTSE Global 100
Greece	Te DAX	Slovakia	SAX		FTSE Acord Glob
	Athens Gen	Slovenia	SBI TOP		FTSE E 300
Hong Kong	Hang Seng	South Africa	FTSE/JSE All Share		FTSE Eurofirst 80
	HSE China		FTSE/JSE Top 40		FTSE Eurofirst 100
	Enterprise	South Korea	FTSE/JSE All Share		FTSE Gold Min
	HSCC Red Chip		FTSE/JSE Top 40		FTSE All World
Hungary	Bio	Spain	IBEX 35		FTSE World
India	BSE Sens	Sri Lanka	CSE All Share		MSCI All World
	S&P CNX 500	Sweden	OMX Stockholm 30		MSCI ACWI Fr
Indonesia	Jakarta Comp	Switzerland	SMI Index		MSCI Europe
Ireland	ISEQ Overall				MSCI Pacific
Israel	Tel Aviv 100				S&P Global 1200
					S&P Europe 350
					S&P Euro

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iShares MSCI

- Country-specific baskets of stocks designed to replicate the country indexes of 22 countries.
- iShares are exchange-traded funds that trade on the American Stock Exchange and are subject to U.S. SEC and IRS diversification requirements.
 - Low cost, convenient way for investors to hold diversified investments in several different countries.

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Factors Affecting International Equity Returns

- Macroeconomic factors
- Exchange rates
- Industrial structure

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Macroeconomic Factors Affecting International Equity Returns

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

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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.

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Industrial Structure

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

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Summary

- This chapter provides an overview of international equity markets.
- A considerable amount of discussion was devoted to differences in secondary equity market structures.
- Cross-listing of a company's shares on foreign exchanges was extensively discussed.
- A variety of international equity benchmarks was also presented.
- Several empirical studies that tested for factors that might influence equity returns indicate that domestic factors, such as the level of domestic interest rates and expected changes in domestic inflation, as opposed to international monetary variables, had the greatest effect on national equity returns. Industrial structure did not appear to be of primary importance. Equity returns were also found to be sensitive to own-currency exchange rate changes.

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