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The Quality of Financial Information and Stock Market Development: A Panel Data Study for the European Economies

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Abstract

The main aim of the paper is to investigate whether the quality of financial information facilitates and promotes the stock market development. We test this hypothesis by using a sample of 36 European economies in the period 2006–2012 based on dynamic panel regression (system GMM) approach. The strength of auditing and reporting standards (SARS) is used as a measure of financial information quality, while the stock market capitalization relative to GDP measures the stock market development. The estimated results demonstrate positive and

significant relationship between financial information quality and capital market development after controlling for the standard macroeconomic and financial specific stock market determinants, suggesting that financial reporting quality is one of the most important determinants of stock market development in European economies. The effects of financial reporting to stock market development are much more significant in the case of non-EU countries. Additionally, the results suggest that growth rate, foreign direct investment, banking sector and corporate governance quality are positively and significantly associated with stock market development, while inflation rate and stock price volatility as measures of macroeconomic and stock price instability have negative influence on stock market activity.

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