

DOCTORAL PROGRAMME

ESSAYS ON THE INFLUENCE OF CULTURE ON EQUITY MARKETS

By

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## **Essays on the influence of culture on equity markets**

### **Thesis abstract**

Public equity markets enhance access to capital for firms. This thesis examines the role of culture in the development of public equity markets in a cross-country setting. Aggarwal et al. (2014a) and Nadler et al. (2019) point out that there is limited research exploring the role of national culture on finance and that more work is required to understand how financial markets and decisions are affected by national culture and formal institutions. This dissertation is formed of five chapters. Chapter one introduces and integrates the dissertation work. We structure our main chapters around the following issues:

In Chapter 2 (Essay 1), we use a cross-country panel data of 55 countries for the period 1995 to 2018 to explore the role of Hofstede's cultural dimensions (Hofstede, 1980) on the development of public equity markets. The focus in Essay 1 is on the main stock exchange (or the main board) of a country, and we examine the impact of national culture on the market capitalization and total capital raised on the equity markets. The main stock exchange is the dominant stock exchange of the country where the large and medium scale enterprises are listed. We find that national culture helps explain the differences in the development of the equity markets across countries after controlling for macroeconomic and formal institutional variables. Specifically, countries with high uncertainty avoidance and high individualism negatively influence the development of equity markets. Further, high cultural distance from the ideal country profile negatively affects the development of public equity markets.

Literature indicates that the impact of financial development and formal institutions on firms depends on the size of the firm (e.g., Beck et al., 2005; Crouzet et al., 2020). In Chapter 3 (Essay 2), we explore if national culture has a differential impact on the development of public equity markets for small firms (as compared to equity market for large firms). We use SME

exchanges as a unique setting to test for this differential impact. SME exchanges are market platforms for small entrepreneurial firms to raise equity capital. Using cross-country panel data of 30 countries for the period 1995 to 2018, we find that national culture has a stronger influence on the development of SME exchanges as compared to the main exchanges. Specifically, high long term orientation has a positive effect, while high individualism and high cultural distance have a negative effect on the development of public equity markets for small firms.

In Essay 1 and Essay 2, we find empirical evidence that aggregate market capitalization, as well as equity capital raised by firms in the exchanges, is lower in countries that are high on the uncertainty avoidance dimension of national culture. In Chapter 4 (Essay 3), we examine the impact of formal institutions in mitigating the effects of high uncertainty avoidance on equity market development for small firms. Since national culture evolves at a slow pace, we need to consider alternative ways to mitigate the potential negative effect of cultural dimensions on the development of equity markets. We analyze the role of formal institutions in mitigating the potential negative effects of high uncertainty avoidance using the New Institutional Economics theory (Williamson, 2000). We use a panel dataset of public equity market for small firms using data on SME Exchanges in 31 countries in this study. The results suggest that strong formal institutions help mitigate the negative effect of high uncertainty avoidance on small firm's access to equity. Further, we find that different formal institutions have a varied influence in mitigating the impact of high uncertainty avoidance in public equity markets for small firms. Further, the negative effect of uncertainty avoidance on the market for equity for small firms is reduced in countries with strong governance-related institutions only in the presence of a better institutional environment such as property rights.

We present our conclusions and key insights in the fifth chapter.