

EFFECT OF FINANCIAL MARKET INTEGRATION ON FOREIGN PORTFOLIO INVESTMENT DIVERSIFICATION IN DEVELOPING STOCK MARKETS

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ABSTRACT

The purpose of this study was to analyze the effect of financial market development level on foreign portfolio investment diversification in developing stock markets. The study sought to affirm or reject the alternative hypotheses that financial market integration level has a negative effect on international portfolio investment diversification. From a sampling frame of 43 developing stock markets, the study constituted a sample of 20 markets through non-probability multi-stage procedures. Using a data capture sheet, equity time series data was collected and summarized into Roy's Safety-First Ratio (RSFR) excess returns on a benchmark of FTSE 100. Data analysis techniques involved were simple pairwise correlation and Johansen cointegration to respectively measure short run and long run integration levels. The study found financial market integration partly critical to international portfolio investment diversification.

Keywords: Integration, Diversification, Developing markets.