UNC KENAN-FLAGLER BUSINESS SCHOOL

How Integrated are Corporate Bond and Stock Markets?

Mirela Sandulescu

Discussant: **Andrei S. Gonçalves**

2021 CICF

Outline

The Paper in a Nutshell

- No-arbitrage $\Rightarrow \mathbb{E}[M_t \cdot R_t] = 1$ with $M_t = a + b^{'} R_t$
- Market integration implies:
- Insight: test for market Integration empirically with
- Frictions (e.g., proportional transaction costs):

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Cross-Market Pricing Errors (in Monthly BPS)

- Pricing errors are comparable with typical trading costs
- Conclusion:
  "This evidence supports the idea that the stock and bond of the same issuer are integrated, and compatible with a notion of no-arbitrage with transaction costs."

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	Credit Rating	Duration	Size	Value	Leverage	Momentum	Asset Growth	Profitability	Liquidity	Short Interest
$\mathbb{E}[M_B R_S] - 1$	9 (0.042)	16 (0.051)	-14 (-0.063)	-8 (-0.027)	25 (0.087)	-9 (-0.059)	10 (0.051)	4 (0.023)	13 (0.028)	18 (0.046)
$\mathbb{E}[M_S R_B] - 1$	-40 (-0.409)	-55 (-0.854)	-30 (-0.181)	-51 (-0.287)	-71 (-0.253)	-73 (-0.406)	-26 (-0.215)	-56 (-0.319)	-27 (-0.204)	-55 (-0.170)

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	(0.430)	(0.835)	(0.534)	(0.197)	(0.099)	(0.270)	(0.350)	(0.209)	(0.427)	(0.216)
$\mathbb{E}[M_S R_B] - 1$	-53	-68	-47	-42	-46	-64	-51	-51	-52	-40
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Final Remarks

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Miscellaneous Comments

- Link to Intermediary-based Asset Pricing
  - Constrained SDFs reflect their respective overall markets (Figure 6)
  - So, link between SDFs and intermediary capital risk factor is hard to interpret
  - I would drop that part of the analysis
- With weak factors (Giglio, Xiu, and Zhang (2021)), results can suggest segmentation when none is present (risk factors just differ across asset classes). Does not matter for your findings, but makes it hard to generalize the method.
- Small notation issue: $M_t = a + b^{'} R_t$ can only be written as $M_t = \omega^{'} R_t$ if you include in R_t a risk-free payoff

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