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ORIGINAL ARTICLE

Emerging capital market efficiency: a comparative analysis of weak-form efficiency in Romania and Hungary in the context of the global financial crisis

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Abstract This paper examines in a comparative manner the weak-form efficiency in the case of two emerging capital markets, the Bucharest Stock Exchange and the Budapest Stock Exchange, in the context of the global financial crisis. The study includes both a theoretical part and a section of original research. Efficient market hypothesis has been an important and widely accepted issue of classical finance for a long period of time. An emerging capital market, like the Bucharest Stock Exchange or the Budapest Stock Exchange, is characterized by deep functional, structural and institutional dysfunctions. The analysis on which this article is built is based on the daily price of Bucharest Stock Exchange indices: BET and BET-C, as well as on daily price of Budapest Stock Exchange indices: BUX and BUMIX during the period of January 2007 to November 2011.

Keywords Efficient market hypothesis · Emerging capital markets · Index · Models · Financial crisis

1 Introduction

This article presents an exhaustive analysis of the efficient market hypothesis in terms of emerging capital markets. Previous empirical studies have revealed the fact that, in general, emerging capital markets are not efficient in semi-strong form or strong form. Specifically, even the weak-form efficiency is very rarely fulfilled on this particular capital market category. Emerging capital markets are very different (Eichengreen and Mody 1998), and not only apparently, compared to developed markets.

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The main contribution of this study is to test the existence of weak-form efficiency of an emerging capital market, such as Bucharest Stock Exchange and Budapest Stock Exchange. The analysis is based on the daily price covering the period January 1, 2007–November 30, 2011 of the most representative Bucharest Stock Exchange indices, namely BET and BET-C. Concomitantly, the empirical analysis provided by this study is based on daily prices covering the same period for BUX and BUMIX index, which are the main indices of Budapest Stock Exchange (Birău 2012a).

Unequivocally, the extreme movements in stock prices over the period under review have raised serious suspicions about the efficient market hypothesis in the case of emerging capital markets, such as Bucharest Stock Exchange and Budapest Stock Exchange. In fact, a significant contribution to highlighting the limits of capital market efficiency is due to the current financial crisis period which is characterized by severe financial imbalances and anomalies.

The advantages assumed by the status of emerging market comprise primarily the huge potential for growth that they hold (Aizenman 2005), which increases the attractiveness for investors (Mody 2004), and also, paradoxically, even the main limits may be viewed as potential opportunities. Thus, the existence of economically or financially underdeveloped structures may be from a certain point of view a real opportunity for a potential investor.

2 Emerging capital markets

An emerging capital market is distinguished by certain key features such as: great return expectations, sharp volatility