THE INFLUENCE OF SOCIAL AND MAINSTREAM MEDIA ON STOCK PRICE SYNCHRONICITY IN CHINA

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dx.doi.org/10.18374/JIFS-22-1.1

ABSTRACT

In this study, we aim to explore the influence of social and mainstream media on stock return comovement in China. The impact of mainstream media on stock price comovement is influenced by social media and vice versa. We generally hypothesize that mainstream and social media interact and then impact stock price synchronicity. We choose 13,745 listed Chinese companies to run our tests. The results suggest that our hypothesis is supported. Our finding supports information-based theory.

Keywords: *Mainstream Media, Social Media; Stock Return Comovement/Stock Price Synchronicity; Information-based theory; Sentiment-based theory*

1. INTRODUCTION

Scholars have devoted substantial effort to understand the determinants of the random movement in stock market prices (Keynes, 1936). A common hypothesis is that firms' information influences stock prices (e.g. Ball and Brown 1968; Watts and Zimmerman 1986 etc.). Two theories are suggested to explain stock price movement. The information-based theory suggests that in a "perfect" (i.e. frictionless) economy with "perfectly" rational investors, stock price equals fundamental values of firms, and thus, any comovement in prices is due to the comovement in fundamentals (Barberis, Shleifer, & Wurgler, 2005). The opponents of the information-based theory argue that investors are not always perfectly rational and the economy is not perfectly frictionless and thus comovement in prices cannot be explained by the comovement in fundamentals solely, and some other variables related to investors may play roles as well. This theory is called sentiment-based theory.

Both theories have received some support. Some studies find that stock return synchronicity is negatively associated with firm-specific information, which are in favor of the information-based interpretation of stock return comovement. When firm information is difficult to reach the public, the lack of information transparency causes high stock comovement, (e.g. Morck, Yeung, and Yu (2000), Jin and Myers (2006), and Dang, Moshirian, and Zhang (2015)). When more firm-specific information is available to investors (i.e. stock prince informativeness is higher), investors do not buy or sell individual stocks following the trend of the entire market and thus lead to higher stock price variability, which means that stock price comovement is negatively correlated with stock price informativeness (e.g. Haggard, Martin, and Pereira, 2008; Hutton, Marcus, and Tehranian, 2009). However, the findings of some other studies suggest the opposite: companies stock price comovement and firm-specific information are positively associated. When more firm-specific information is incorporated into stock prices rapidly, companies have higher stock price comovement. They argue that stock price comovement increases when transparency improves because stock price volatility reduces as rapid information is incorporated into stock price (e.g. West 1988; Dasgupta, Gan, and Gao 2010; Kan and Gong 2017). The inconsistency in this line of research motivates us to investigate this issue further.

Firms use either mainstream or social media to release firm-initiated information (Miller 2006; Bushee and Miller 2012; cited by Blanksespoor, Miller, and White, 2014). News influence investor's judgment and decisions and that impacts stock price movement (e.g. Cutler, Poterba, and Summers, 1989; Tetlock, 2007). In western countries, government is not allowed to own and run media. However, in China, Chinese mainstream media is owned and ran by the government directly or indirectly and Chinese social medias