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Excess stock return comovements and the role of investor sentiment

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Abstract

This paper investigates whether investor sentiment can explain stock return comovements. Our findings demonstrate that since the 1960s, there has been a clear and rapid increase in correlations between international equity markets. Decomposing the equity returns into fundamental and non-fundamental components reveals that the increased correlation is driven by the non-fundamental part. We find that stock return comovements are mainly driven by investor sentiment, which explains the level, variance, and covariance of the non-fundamental component of returns.

JEL Codes: C32; G15.

Keywords: Excess Comovement; Investor Sentiment; International Equity Markets.

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