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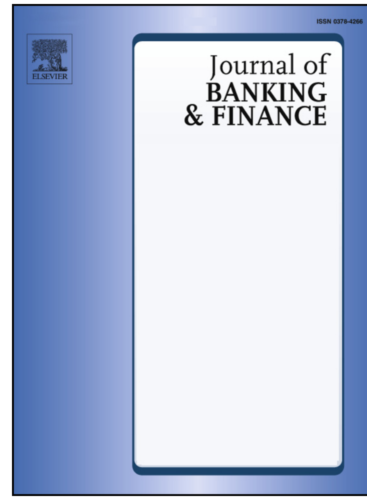

Costs and benefits of financial regulation: Short-selling bans and transaction taxes

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Costs and benefits of financial regulation: Short-selling bans and transaction taxes

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Abstract

We quantify the effects of financial regulation in an equilibrium model with delegated portfolio management. Fund managers trade stocks and bonds in an order-driven market, subject to transaction taxes and constraints on short-selling and leverage. Results are obtained on the equilibrium properties of portfolio choice, trading activity, market quality and price dynamics under the different regulations. We find that these measures are neither as beneficial as some politicians believe nor as damaging as many practitioners fear.

Keywords: Financial regulation; portfolio management; market microstructure.

JEL classification: D53; G18; C63.

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