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Impact of short selling activity on market dynamics:  
Evidence from an emerging market

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**Abstract**

With unique daily short sale data of Borsa Istanbul (stock exchange of Turkey), we investigate the dynamic relationship between short selling activity and volatility, liquidity and market return from January 2005 to December 2012 using a VAR( $p$ )-cDCC-FIEGARCH(1, $d$ ,1) approach. Our findings suggest that short sellers are contrarian traders and contribute to efficient stock market in Turkey. We also show that increased short selling activity is associated with higher liquidity and decreased volatility. However this relation weakens during the financial turmoil of 2008. Our results indicate that any ban on short sales may be detrimental for financial stability and market quality in Turkey.

*Keywords:* short selling, contrarian trading, financial stability, market quality, dynamic conditional correlation

*JEL:* C51, G11, G14, G18

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