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Micro(structure) before Macro? The Predictive Power of Aggregate Illiquidity for Stock Returns and Economic Activity

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Abstract

This paper constructs and analyzes various measures of trading costs in US equity markets covering the period 1926–2015. These measures contain statistically and economically significant predictive signals for stock market returns and real economic activity. We decompose illiquidity proxies into a component capturing aggregate volatility and a residual. The predictive content of these components differs in important ways. Specifically, we find strong

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