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Financial Markets Integration between Morocco and France: Implications on International Portfolio Diversification

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Abstract : This paper examines equity market integration between Morocco and France and its consequent implications on international portfolio diversification. In the absence of stock market linkages, Morocco can act as a diversification destination to European investors, allowing higher returns at a comparable level of risk in developed markets. In contrast, this attractiveness is limited if both financial markets show significant linkage. The research empirically measures financial market's integration in by capturing the conditional correlation between the two markets using the Generalized Autoregressive Conditionally Heteroscedastic (GARCH) model. Then, the research uses the Dynamic Conditional Correlation (DCC) model of Engle (2002) to track the correlations. The research findings show that there is no important increase over the years in the correlation between the Moroccan and the French equity markets, even though France is considered Morocco's first trading partner. Failing to prove evidence of the stock index linkage between the two countries, the volatility series of each market were assumed to change over time separately. Yet, the study reveals that despite the important historical and economic linkages between Morocco and France, there is no evidence that equity markets follow. The small correlations and their stationarity over time show that over the 10 years studied, correlations were fluctuating around a stable mean with no significant change at their level. Different explanations can be attributed to the absence of market linkage between the two equity markets.

Keywords : equity market linkage, DCC GARCH, international portfolio diversification, Morocco, France
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