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Election Effect in Malaysian Stock Market: The Case of "Trump Effect"

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Abstract – **The United States Presidential Election in 2016 is marked as one of the historic election in the modern political history as Donald Trump's shocking win raises political risk surrounding the global economy. Amidst the political uncertainties, it is the aim of this study to investigate the presence of this political election effect on the Malaysian stock market. This study observes the existence of abnormal returns of the Kuala Lumpur Composite Index (KLCI) and its 30 constituents, and measures the magnitude of the abnormal returns. This study uses Augmented Dickey-Fuller test to identify the stationary of the data and Ordinary Least Square method to analyze the relationship between the election and the stock returns. The unit root test of the data displays that each variable is stationary at level form. Overall, findings show that the Malaysian stock market is negatively affected by the election as the KLCI slipped by 1% during the Election Day. Six out of thirty constituents of KLCI displays similar negative results with SapuraKencana exhibits the lowest index return. This inferred that the Malaysian stock market is a semi-strong efficient market and is affected by the external general election.**

Keywords – **Election effect, stock market, Kuala Lumpur Composite Index, market efficiency.**

I. INTRODUCTION

Political election effect in the stock market is one of the renowned topics that are still debated among researchers and academics from financial economics streams in unveiling the existence of market anomaly. Election effect falls under the study of the calendar effect, which denotes the shift in security prices in stock market portraying selected trends on seasonal occasion [1]. Calendar effect is also referred to as calendar anomalies which defines the occurrence of recurring patterns or trends happens at a specific time or consistent interval corresponding to a calendar year [2]. Stock market participant owns an advantage in beating the market by detecting the patterns of such anomalies thus; these anomalies are regarded as threats to the market efficiency concept. The presence of anomalies violates the fundamental assumption of efficient market hypothesis (EMH) which defines that all available information should be absorbed by the stock prices in the market at any given point in time, disallowing the participant from beating the market and earns excessive profit [1]. Calendar anomalies are of various types, namely Weekend effect, January effect, Friday the 13th effect, monthly effect, Day of the week effect, turn of the month effect and turn of the year effect [3]. Other related anomalies include Holiday effect, where Christmas and New Year effect show significant effect on the stock market [4]. Apart from these existing calendar anomalies, several researchers set forth their opinions to claim that the political election holds substantial influence in stock market performance [5] - [7] and this study intends to investigate this election effect in detail.

Politics and investor behavior relationship has been researched in many countries and in diverse contexts. Past studies suggest that the political risk around elections initiates economic uncertainty that elevate the risk aversion behavior among investors. The most recent example of this political uncertainty can be observed through the 58th quadrennial United States presidential election. Donald Trump's success in the US presidential election received a mixture of shock, disbelief and anxiety from the media all across the globe. America, being one of the world's most powerful economies, the election results are expected to affect not only the country alone, but the repercussions are going to be evident on a global level. The Asian markets seemed to be affected with a greater impact in response to the American presidential cycle compared to the American stock market performance [8]. Beginning from the year of 1988, during the first-year American presidency (or post-election years) and pre-election years, Malaysian stock market experienced maximum returns during US pre-election years followed by post-election years where KLCI climbed 16 percent on average during the former years. In view of Malaysia's large trade sector, Trump's apparent nationalist tendencies as displayed in his manifesto may bring about unfavorable policies which would affect Malaysia's economy negatively. Due to the rising of political risk encircling the United States political election, this study aims to examine the presence of election effect in Malaysian stock market during the United States 2016 Presidential Election by analyzing the efficiency of the Malaysian stock market in dealing with such event. This paper is organized as follows. In section 2, discussion on political election effect is provided. Section 3 provides an explanation on data

and methodology. The results and discussion are presented in section 4. Finally, our work of this study is summarized in the last section.

II. POLITICAL ELECTION EFFECT

Researchers from investment institution and academics from financial streams are dedicated to unearth the existence of stock market anomalies. Providing abundant market anomalies, the effect of political election has appealed their persistent attention. Some researchers claim that the national political election holds a significant stimulus towards the performance of the stock market. The existence of political business cycle could be primarily observed through US market as this cycle demonstrates the propensity of the controlling party in amending the government policies throughout the presidential term [9]. For the early duration of the presidential term, the government often initiates with proportional austerity whereas ends with monetary simulative expansion prior elections. The government spending expansion is capable in stimulating the market and consequently forming a decent image of the governing party in return [10].

Different finding discovers that a change in political parties in America, Japan, Britain and France respectively leads to a negative relationship to stock returns [11]. In other word, a change in governments leads to a decline in stock market returns. This may due to different economic agendas by different political parties resulting to frequent economic policy modification. Investors regard this scenario as serious uncertainty and majority of them opt for conservative stocks in order to protect their positions. In similar point of view, the stock market can be influenced by a switch in government administration [12]. The reason is that new governments would often implement new fiscal and monetary policies, leading to an increase in uncertainties. The uncertainty discourages investors from taking risk, which causes negative stock returns. This is in line with partisan theory that suggests dissimilar economic rules and policies are designed resembling the preference of political parties [13]. Price stability would be put as a more serious issue for business-oriented parties compared to the unemployment problem. Contrariwise, parties with labor-orientation would lean towards employment matter rather than inflation.

The conclusion of different partisan parties gives different impact on the stock market is supported by the evidence of stock market return performed well in the Australian stock market when Liberal National ministries were in the position of the national government compared to Labor ministries [14]. From the perspective of general election, the Athens Stock Exchange (ASE) shows certain reaction and is significantly affected by the national general election [15] whereas significantly higher stock returns of New Zealand Exchange are found during 2002 general election [16]. Furthermore, the existence of significant election effect before and after the event is signified from the two latest Malaysia's general elections which held in 2008 and 2013 [7]. Competitive fight between two main political players in Malaysia's politic arena created political uncertainties causing a negative and significant role in affecting the return of the stock market. However, some researchers prove the absence of the political cycle in Malaysian stock market returns, although the volatilities of the Malaysian stock market with respect to political cycle are shown to be empirically significant [17].

Massive and different approaches of research have been done in examining the effect of a country's election towards its stock market. This study, on the other hand, intends to examine the effect of election of another country, specifically the United States, on the Malaysian stock market. For this particular study, it investigates a single United States presidential election which held in 2016.

III. RESEARCH METHODOLOGY

The study focuses on exploring any significant effect in the Malaysian stock market during the period of US Presidential Election 2016. This study uses daily FTSE Bursa Malaysia Kuala Lumpur Composite Index (FBMKLCI) ranges from the date 19th October 2016 until 30th November 2016. The period chosen consists of 15 trading days before and after the election event. This study uses the empirical model following the regression-based approach [9] with the purpose of analyzing the stock price and FBMKLCI returns during the election event. Ordinary Least Square (OLS) regression with dummy variable is used in this study to see the effect of US Presidential Election 2016 on the Malaysian stock market. This study observes the effect of election on FBMKLCI return as an aggregate, as well as, the effect on firm in specific.

The measure of statistical significance of a relationship between one dependent variable and another independent variable can be obtained from the OLS regression model. This study adopts the log daily returns of stock returns as well as stock market returns, Kuala Lumpur Composite Index (KLCI) as the dependent variable to be regressing in order to identify any significant election effect. Daily stock prices and the daily KLCI are converted into daily logarithmic return as follows:

$$R_t = 100 \times [ln(l_t) - ln(l_{t-1})] \qquad (1)$$
where
R_t = stock index return at time t
l_t = stock price of firm at time t
l_{t-1} = stock price of firm at time $t-1$
ln = natural logarithm.

Daily returns were calculated for all 30 companies as well as the KLCI from 19th October 2016 until 30th November 2016. The regression equation is illustrated as follows:

$$R_t = \beta_i D_{it} + \varepsilon_t \qquad (2)$$
where
R_t = stock index returns at time t
β_i = mean return attributable to ith characteristics
D_{it} = dummy variable that takes the value of 1 if the tth observation falls on the event day, and 0 otherwise
ε_t = error term

The dummy variable is set to 1 on the event day, and 0 for the fifteen days before and after the event. In this particular study, the 9th November 2016, which falls on Wednesday, representing the dummy variable is set to 1. Although 8th

November 2016 was the date of the 58th US Presidential Election, the effect of this election should be observed the day after due to difference in time zone between Malaysia and the United States, where the result of the election is announced at 4pm Malaysian time. For the fifteen preceding trading days as well as the following subsequent fifteen trading days after the election event, the dummy variable is denoted by 0. Ordinary Least Square (OLS) regression with dummy variable is implemented to identify whether the event of 58th quadrennial US presidential election demonstrates its effect on the daily returns of the Malaysian stock market as a whole or by firm-specific. Thus, the hypothesis tested in this study is as follows:

1) $H_0: \beta_i$ = no abnormal return on the Malaysian stock market during the US Election 2016

2) $H_1: \beta_i$ = there is abnormal return on the Malaysian stock market during the US Election 2016

IV. RESULTS AND DISCUSSION

Table I displays the result of regression on the effect of the 2016 US Presidential Election on Malaysian stock market.

TABLE I
RESULT OF REGRESSION OF THE EXISTENCE OF ELECTION EFFECT

Variables	Coefficient (%)		Standard Error	t-statistic	p-value
KLCI	-0.009128	*	0.004516	-2.021406	0.0526
AMBANK (1015)	-0.025625	***	0.011301	-2.267417	0.0310
ASTRO (6399)	-0.031058	*	0.015739	-1.973342	0.0581
AXIATA (6888)	-0.023004		0.016224	-1.417928	0.1669
BAT (4162)	-0.006460		0.017626	-0.366527	0.7166
CIMB (1023)	-0.010923		0.014448	-0.756031	0.4557
DIGI (6947)	-0.003231		0.006463	-0.499878	0.6209
GENM (4715)	-0.014635		0.016714	-0.875647	0.3884
GENTING (3182)	-0.027327	*	0.013985	-1.954001	0.0604
HAPSENG (3034)	0.001623		0.005532	0.293420	0.7713
HLBANK (5819)	-0.006432		0.004628	-1.389875	0.1751
HLFG (1082)	0.001520		0.009001	0.168917	0.8670
IHH (5225)	-0.004119		0.008020	-0.513616	0.6114
IOICORP (1961)	-0.020057	***	0.006783	-2.957157	0.0061
KLCC (5235SS)	-0.000495		0.009125	-0.054196	0.9572
KLK (2445)	-0.011210		0.006712	-1.670308	0.1056
MAXIS (6012)	-0.001524		0.012352	-0.123412	0.9026
MAYBANK (1155)	-0.010709		0.012927	-0.828452	0.4142
MISC (3816)	-0.000318		0.748185	-0.000425	0.9997
PBBANK (1295)	-0.005977		0.003725	-1.604605	0.1194
PCHEM (5183)	-0.006062		0.513710	-0.011801	0.9907
PETDAG (5681)	0.002314		0.006221	0.372002	0.7126
PETGAS (6033)	-0.000693		0.007109	-0.097426	0.9231
PPB (4065)	-0.005472		0.008758	-0.624805	0.5370
RHBBANK (1066)	-0.001531		0.017246	-0.088787	0.9299
SAPURA ENERGY (5218)	-0.049861	***	0.014889	-3.348812	0.0023
SIME (4197)	-0.015265		0.013253	-1.151740	0.2588
TENAGA (5347)	-0.002047		0.003666	-0.558173	0.5810
TM (4863)	-0.000433		0.007176	-0.060278	0.9523
WPRTS (5246)	-0.017265	**	0.008144	-2.119976	0.0427
YTL (4677)	0.000556		0.016700	0.033270	0.9737

*** Denotes statistical significance at the 1% confidence level.
** Denotes statistical significance at the 5% confidence level.
* Denotes statistical significance at the 10% confidence level.

From the aggregate perspective, Kuala Lumpur Composite Index (KLCI) displays a negative and significant return during the election event, which is a decline of 0.9128%. Subsequently, the negative return or the effect can be seen in all 29 companies except for the stock prices return of Petronas Dagangan Bhd., which displays the positive but insignificant return. The nation's benchmark FTSE Bursa Malaysia KLCI slipped 1% to 1,647.62 points resulting from Trump's win of the election, its lowest level since July 8 and its worst single-day decline in over a month [18]. The presence of election effect is consistent with previous research findings [7].

These findings reject the null hypothesis supporting the existence of election impact on the Malaysian stock market. As Malaysia is seen to build a firm economic bond with the United States government, any changes in the political climate may affect the Malaysian economy. One possible explanation for the presence of election effect is due to the sentiment of global investor which is largely induced by issues related to American politics affecting smaller and less liquid markets in Asia. Smaller absolute amount of funds invested or withdrawn can have a far greater impact than in bigger markets. Therefore, positive or negative sentiment in the US with respect to elections plays out in Asian markets more than it does in the US [8].

Observing through firm-specific, the results show that there are 6 companies that are significantly affected by the election event. This includes AMMB Holdings Berhad with a negative return of -0.025625%, IOI Corporation with -0.020057%, Astro with -0.031058% and Genting with -0.027327%. SapuraKencana records the lowest return with -0.049861%, while Westport displays the opposite (-0.017265%) as compared to other 5 affected companies. In contrary, other 24 listed companies show insignificant result of the election effect on the stock prices.

The global markets were rattled after Republican nominee Donald Trump beat his Democrat rival Hillary Clinton to become the 45th President of the United States. As a result, Malaysian market is viewed to be affected by the global market as the ringgit skid 0.5% to 4.22 ringgit against the dollar, its lowest level since the first month of

2016. The fall of Malaysian currency has been predicted by many research analysts stating that ringgit is projected to weaken to 4.50 against the greenback if Donald Trump is victorious [18]. Furthermore, AmBank states that the company will cut its target for the end-2017 for the FBMKLCI to 1,645 points if Trump is elected as the new president of the United States [19]. Weakening of the national currency has negatively affected financial institution and banks, including AMMB Holdings Berhad.

In addition, SapuraKencana Petroleum Berhad, a leading global integrated oil and gas services and solutions provider shows a decline in return, slumped 5.1% to 1.48 ringgit because of the overall market weakness and also falling of crude prices. Benchmark oil prices fell overnight following the news of Donald Trump's victory in the U.S. presidential race. Brent crude was down 1.1% at $45.53 a barrel Wednesday, its lowest levels since early August [20]. SapuraKencana Petroleum is one of the major losers and is significantly affected by the election event. Other major loses include gaming conglomerate Genting and television service provider Astro Malaysia, slipping 2.6% to 7.8 ringgit and 3.2% to 2.72 ringgit [20].

Westports Holdings Berhad, the major player in the Asian logistic industry is observed to be negatively affected by the election event. This may due to the pressure from inward looking policies as announced by Trump during his manifesto. Trump's campaign promises could possibly put a dent on Free Trade Agreement (FTA)s, including North American Free Trade Agreement (NAFTA) and Trans Pacific Partnership (TPP). The new elected president may even impose trade barriers against China over concerns on excessive government subsidies, currency fixing and US intellectual property usage. These will unsettle global trade, and thus could negatively impact the logistics and shipping businesses in the long term [21].

Malaysia is a leading palm oil producer and the news on Trump's victory has led to a jump of palm oil price to a four-year high as the Malaysian ringgit in the face of a sell-off in emerging market currencies. IOI Corporation Berhad however, experience a decline in return due to the election event. This may due to the fall in exports of palm oil. Export of palm oil to US represents 4% of total export [21]. Even though the figure is small, a decrement in export would give an impact to the palm oil industry. In contrariwise, Petronas Dagangan was the only index stock to close higher, rising 0.2% to 23.4 ringgit after it reported an increase in third-quarter profit. The unexpected outcome of Trump's winning the election directs investors scurrying for traditional safe-haven assets, as markets brace for a period of prolonged uncertainty given Trump's controversial stance on foreign matters and trade policies.

V. CONCLUSION

The aim of this study is to investigate if there are abnormal returns in Malaysian stock market during the period of US Presidential Election 2016 and to measure the magnitude of the return if abnormal return exists. The OLS regression model is adopted to investigate the significance of the independent variables on the dependent variable. The overall finding indicates that the 58th quadrennial presidential election shows a significant and

negative impact on the Malaysian stock market as an aggregate. 6 out of 30 listed companies are significantly affected and exhibit negative return. They are AMMB Holdings Bhd., Astro Malaysia Bhd., Genting Berhad, IOI Corporation Bhd., SapuraKencana Petroleum Bhd. and Westports Holdings Bhd. KLCI has turned down by 0.09128% and SapuraKencana with the lowest index return declines by 0.04981%. The results signify that Trump's shocking win has definitely raised uncertainties across the global from the perspective of politics and economics. Malaysian stock market is not excluded to face the effect of this historic election as the stock market exhibits a semi-strong form efficiency when information on market data and publicly available information related to the external general election are reflected in the price of stocks.

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