Economics Bulletin

Volume 28, Issue 5

Research Announcement

Arbitrage and Dynamic Asset Pricing

AROURI Mohamed El Hedi
MODEM University of Paris X Nanterre

Abstract

This paper investigates the determinants of stock returns in the French stock market in an Arbitrage Pricing Theory framework. The analysis is conducted with monthly data from the French stock market over the period 1990-2001. Financial theory predicts that a set of macroeconomic variables systematically affect stock market returns such as : industrial production, expected and unexpected inflation, the spread between long and short interest rates and unemployment rate. We estimate the regressions using the Kalman filter, under the hypothesis that the agent's expectations are adaptive rather than rational. This method allows us also to work under the more realistic assumption of time-varying sensitivities and risk premium. We find that a two to four- factor structure is appropriate to explain stock returns. The results also show that the factor structure changes from an equity to an other.

Completed draft available on request from:
AROURI Mohamed El Hedi
MODEM University of Paris X Nanterre
mohamed-el-hedi.arouri@u-paris10.fr
200, Avenue de la République
Nanterre, 92001, France

Citation: AROURI Mohamed El Hedi, (2003) "Arbitrage and Dynamic Asset Pricing", *Economics Bulletin*, Vol. 28 no.5 p.A1.
Submitted: November 10, 2003 **Published:** November 10, 2003.
URL: http://www.accessecon.com/pubs/EB/2003/Volume28/EB-03AA0005A.pdf