Abstract

Settlement effects describe the impact from expirations of derivatives on the trading of the underlying market. The settlement effects of index futures may arise from stock index arbitrageurs unwinding of arbitrage positions in the stock market or speculators attempt to gain from futures positions by manipulating the price of stocks. Herd behavior is defined as investors implement an investment strategy based on mimicking other investors’ actions or the market consensus. If the investors mimic the actions of futures arbitrageurs and speculators, the evident herding effects will appear during the period of index futures settlement. This study integrates the two topics of settlement effects and herding effects. The empirical analysis is designed to explore the herding behavior in Taiwan stock market during the period of settlement of index futures. The results show that there are significant herding effects before and after three days to the maturity date. In addition, we find that the herding behavior is significant when the stock prices declines, low trading volume, and high stock market volatility.

Keywords: Index futures, Settlement effect, Herding behavior