R-Squared Around the World: New Theory and New Tests

Li Jin & Stewart C. Myers

SHARE

WORKING PAPER 10453

DOI 10.3386/w10453

ISSUE DATE April 2004

Morck, Yeung and Yu (MYY, 2000) show that R2 and other measures of stock market synchronicity are higher in countries with less developed financial systems and poorer corporate governance. MYY and Campbell, Lettau, Malkiel and Xu (2001) also find a secular decline in R2 in the United States over the last century. We develop a model that explains these results and generates additional testable hypotheses. The model shows how control rights and information affect the division of risk-bearing between inside managers and outside investors. Insiders capture part of the firm's operating cash flows. The limits to capture are based on outside investors' perception of the value of the firm. The firm is not completely transparent, however. Lack of transparency shifts firm-specific risk to insiders and reduces the amount of firm-specific risk absorbed by outside investors. Our model also predicts that opaque' stocks are more likely to crash, that is, to deliver large negative returns. Crashes occur when insiders have to absorb too much firm-specific bad news and decide to give up.' We test these predictions using stock returns from all major stock markets from 1990 to 2001. We find strong positive relationships between R2 and several measures of opaqueness. These measures also explain the frequency of large negative returns.

Download a PDF

Information on access

Acknowledgements and Disclosures

Citation and Citation Data

Published Versions

Jin, Li and Stewart C. Myers. "R2 Around The World: New Theory And New Tests," Journal of Financial Economics, 2006, v79(2,Feb), 257-292.

Related

TOPICS

Financial Economics
Portfolio Selection and Asset Pricing
Financial Markets

PROGRAMS

Corporate Finance

More from the NBER

In addition to working papers, the NBER disseminates affiliates' latest findings through a range of free periodicals—the NBER Reporter, the NBER Digest, the Bulletin on Health, the Bulletin on the Economics of Alzheimer's, and the Bulletin on Entrepreneurship—as well as research spotlights, lectures, and panel videos.

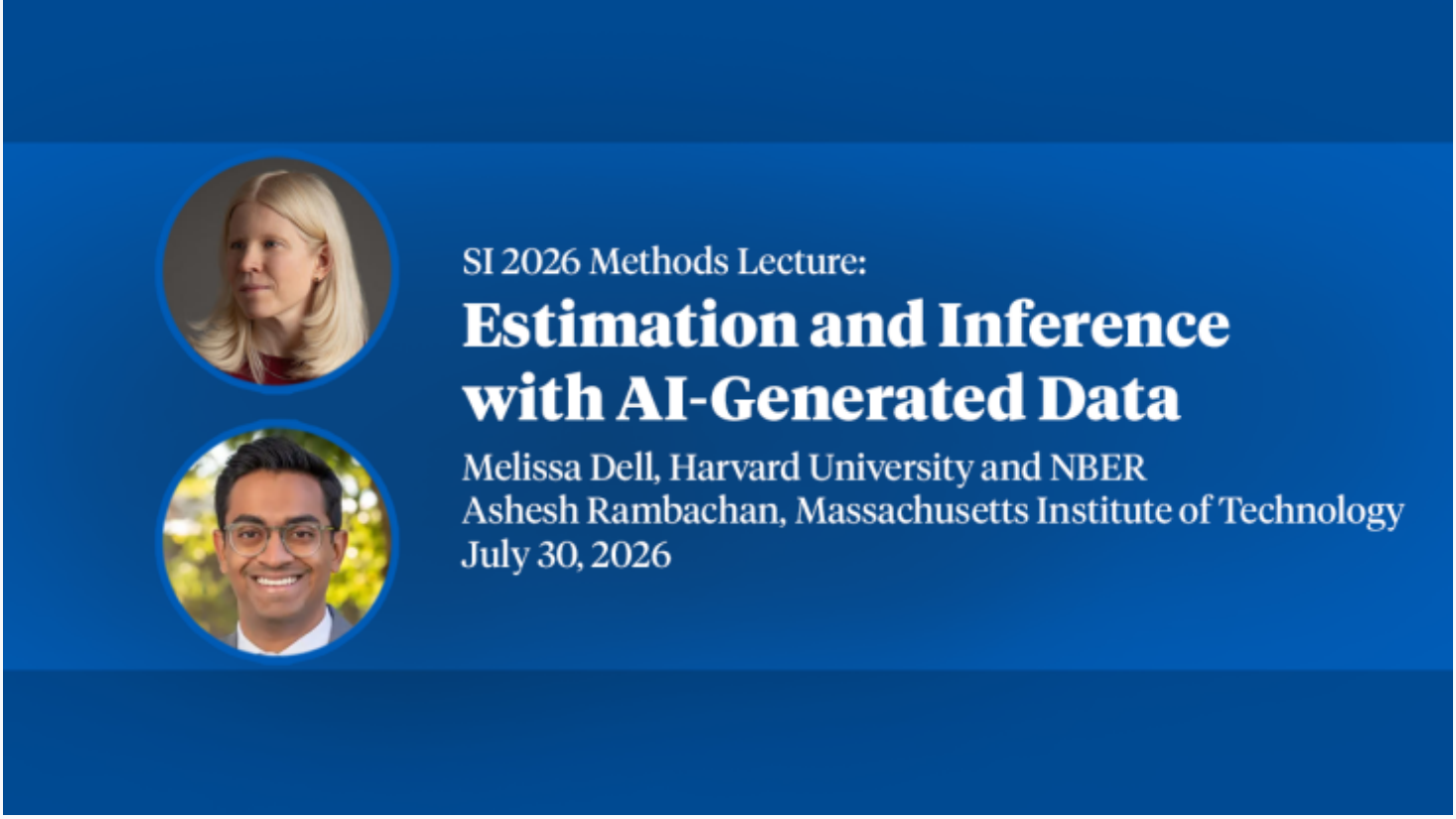


2026, 18th Annual Feldstein Lecture, Mark Duggan, "Social Security Reform in an Era of Fiscal Deficits"

FELDSTEIN LECTURE

PRESENTER: MARK DUGGAN

Mark Duggan, who is currently the Wayne and Jodi Cooperman Professor of Economics at Stanford University and will soon...



2026, Methods Lecture, Melissa Dell and Ashesh Rambachan, "Estimation and Inference with AI-Generated Data"

METHODS LECTURES

PRESENTERS: MELISSA DELL & ASHESH RAMBACHAN

Research Associate Melissa Dell of Harvard University and Ashesh Rambachan of MIT delivered the 2026 Methods...



2026, SI Household Finance, Paul Goldsmith-Pinkham, "Using AI in Household Finance Research: A Practical Guide"

VIDEO

PRESENTER: PAUL GOLDSMITH-PINKHAM

Supported by the Vanguard Group

National Bureau of Economic Research

Contact Us
1050 Massachusetts Avenue
Cambridge, MA 02138
617-868-3900
info@nber.org
webaccessibility@nber.org

© 2026 NATIONAL BUREAU OF ECONOMIC RESEARCH. ALL RIGHTS RESERVED.