

# **THE IMPACTS OF INDEX REBALANCING AND THEIR IMPLICATIONS: THE CASE OF SET50 INDEX**

## **ABSTRACT**

This paper investigates the impacts of inclusions in and exclusions from the SET50 index during 2001 to 2010. The study examines the price, volume and liquidity impacts of SET50 index rebalancing. Moreover, examination on the associations between the changes of liquidity and the observed abnormal return is performed. The main objective is to observe whether stock in Thai market is consistent with the liquidity hypothesis.

The results of the price and volume effects reveal that Thai stocks have downward sloping demand curve. The liquidity effects as well as the relationship of abnormal return and changes of liquidity support the hypothesis of liquidity. I found positive (negative) abnormal return on the announcement date of inclusions (exclusions) stocks in the SET50 index. In longer period shows that both significant positive and negative abnormal returns persist permanently ruling out the hypothesis of price pressure which predicts the price reversion in long-term. The significant increasing in traded volume before the effective day confirms the fact that index funds normally rebalance their portfolio just before the effective date in order to minimize the tracking error. Finally, the investigation in liquidity changes and its relation to the abnormal return from the regression shows the signs of coefficient as expected under assumption of liquidity hypothesis but not all are highly statistical significant.