

Capital Market Development and Corporate Investment

ABSTRACT

This article examines the impact of legal protection on the sensitivity of investment to stock prices in eleven countries of the Asian Pacific region. We use two measures – an indicator for common-law country and an investor protection index – as a proxy for legal protection, and find that investment-price sensitivity is more positive in common-law countries and countries with better investor protection, especially among financially unconstrained (nonequity-dependent) firms. This relation is supported by our empirical finding that stock prices are more informative in common-law countries and countries with better investor protection, while stock price informativeness has been documented to have strong positive effect on the investment-price sensitivity.