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The Impact of Transaction Costs on Turnover, Asset Prices and Volatility: The Cases of Sweden's and Finland's Security Transaction Tax Reductions

ABSTRACT

Drastic changes in transaction tax on securities trading in both Sweden and Finland give us a unique opportunity to study the effects of a purely exogenous change in transaction costs. The impact on turnover can be predicted accurately using a simple model. Lower transaction costs cause significant increases in turnover with an elasticity of approximately -1 . We apply an asset-pricing model that is able to predict asset price changes. The transaction cost elasticity in asset prices is -0.20 for Sweden and -0.21 for Finland. Volatility in securities prices is significantly reduced when transaction costs decrease.

Keywords: Security Transaction Tax, Transaction Cost, Transaction cost elasticity

JEL classification: G12, G28

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