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Do Portfolio Diversification Benefits Exist?
A Study of Selected Developed and Emerging Markets

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Abstract

The objective of the study is to 1) examine the existence of portfolio diversification opportunities and 2) measure the diversification benefits. The study is performed on 14 markets (seven developed and seven emerging markets) covering a period from January 2010 to December 2020. The study is performed on E7 emerging markets (Brazil, China, India, Indonesia, Mexico, Russia and Turkey) and G7 developed markets (Canada, France, Germany, Italy, Japan, UK and USA). The results of correlation, Granger causality, and cointegration tests reveals the lack of short-term and long-term integration among the markets and existence of portfolio diversification opportunities. The study examines portfolio diversification opportunities by comparing non-diversified portfolios (home market) with diversified portfolios (equal weighted portfolios, minimum variance portfolios, and maximum Sharpe portfolio). Investors from developed markets can gain better returns, lower risk, and a higher Sharpe ratio with portfolio diversification in emerging markets. Investors have a significant reduction in their portfolio risk and an increase in their Sharpe ratio with investment diversification.

Keywords: International diversification, portfolio diversification benefits, developed markets, emerging markets, minimum variance portfolio, maximum Sharpe portfolio, equally weighted portfolio

JEL Classifications: G11, G15, F15, F21

1. Introduction

The portfolio diversification opportunities arising from the lack of financial market integration are an important topic of research in finance. Investors are interested in financial market integration because of the potential benefits of portfolio diversification (Click and Plummer, 2005; Patel, 2019a). The integration of equity markets affects the benefits of global divergence and financial reliability (Ibrahim 2005; Patel, 2017). Investors look at diversification as an opportunity to get a better risk-return tradeoff and improve the performance of their portfolio. Due to globalization, international trade, and increasing investments, the integration of financial markets

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