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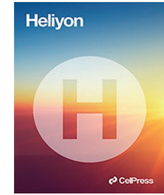

Does the financial flexibility prevent stock price crash risk during COVID-19 crisis? Evidence from the Vietnamese stock market

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ABSTRACT

Stock price crash risk is of particular interest in developing countries as it poses a significant threat to investors and can have detrimental effects on the stability of emerging markets. This study investigates the role of financial flexibility in preventing stock price crash risk in the Vietnamese stock market, with a specific focus on the COVID-19 pandemic. Using the fixed-effect, system GMM, and quantile regression methods on a sample of 645 Vietnamese listed firms from 2011 to 2021, this study found that financial flexibility has a significant impact on preventing stock price crash risk. This effect was augmented during the COVID-19 crisis. Furthermore, this study found that financial flexibility mitigated the impact of the COVID-19 crisis on stock price crash risk. The findings provide important implications for firm regulators, shareholders, and investors to respond to similar future crises.

1. Introduction

Stock price crash risk (SPCR) refers to the likelihood or probability of a significant and sudden decline in the prices of stocks or securities in a financial market [1]. It represents the potential for a rapid and substantial decrease in the value of an individual stock, a specific sector, or even the overall market. It is for this reason that SPCR is a major concern for shareholders, investors, and regulators. Advancements in technology and the rise of algorithmic trading have led to increased concerns about SPCR [2,3]. The use of automated trading systems and complex financial instruments can amplify market movements and potentially contribute to abrupt price declines [4]. In developing countries, the financial system is often fragile, and investor sentiment is strongly affected by market fluctuations [5–8]. Therefore, it is vital to study SPCR in the context of developing countries.

Several studies have attempted to analyze the factors that influence SPCR within different markets. Corporate governance studies have suggested that SPCR is a result of the management holding on to bad news and that SPCR therefore depends on the corporate governance structure of firms. For example, Dang and Nguyen [1] found that a strong board of directors (BOD) can increase SPCR, whereas a good external audit service can reduce such effect. Similarly, Wu et al. [9] found that a favorable corporate governance mechanism helps reduce SPCR in the Taiwanese stock market.

From an economic shock perspective, prior studies have provided evidence of the impact of macro-economic factors on SPCR. Callen and Fang [10] provided evidence that firms headquartered in countries with higher levels of religiosity exhibit lower levels of future SPCR. Xiao et al. [11] found that oil-price uncertainty increases SPCR in Chinese stock market. Similarly, Luo and Zhang [12]

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