Transitional Dynamics of Oil Prices

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## Contents

<table>
<thead>
<tr>
<th>Title</th>
<th>Pages</th>
</tr>
</thead>
<tbody>
<tr>
<td>Public Spending and Economic Growth in Lebanon</td>
<td>8-16</td>
</tr>
<tr>
<td><strong>Ahmad Salloum and Jamal Hayek</strong></td>
<td></td>
</tr>
<tr>
<td>Does External Indebtness Enhance the Incidence of Poverty in Pakistan? An Empirical Evidence</td>
<td>17-23</td>
</tr>
<tr>
<td><strong>Muhammad Ramzan Sheikh and Tanvir Alam</strong></td>
<td></td>
</tr>
<tr>
<td>Transitional Dynamics of Oil Prices</td>
<td>24-30</td>
</tr>
<tr>
<td><strong>Süleyman Hilmi Kal, Ferhat Arslaner and Nuran Arslaner</strong></td>
<td></td>
</tr>
<tr>
<td>Growth &amp; Future Prospects of Currency Derivatives in India</td>
<td>31-43</td>
</tr>
<tr>
<td><strong>Meena Bhatia</strong></td>
<td></td>
</tr>
<tr>
<td>Quality Service and Customer Satisfaction in Micro-Finance Institutions in Ethiopia</td>
<td>44-71</td>
</tr>
<tr>
<td><strong>Bekuretsion Assasahegn Fetene and Eno L. Inanga</strong></td>
<td></td>
</tr>
<tr>
<td>The Effect of Judicial Independence to FDI into Eastern Europe and South Asia</td>
<td>72-77</td>
</tr>
<tr>
<td><strong>Bülent Doğru</strong></td>
<td></td>
</tr>
<tr>
<td><strong>Raisul Islam, M. Talhatul Islam and Sonia Sharmin</strong></td>
<td></td>
</tr>
<tr>
<td><strong>Samih Antoine Azar and Fadi Asrawi</strong></td>
<td></td>
</tr>
<tr>
<td>Analysis of the Interrelationship between the Economies of Laos, China and Thailand</td>
<td>116-127</td>
</tr>
<tr>
<td><strong>Phoukeo Vongvichith</strong></td>
<td></td>
</tr>
<tr>
<td>Lead-lag Relationship between Option Returns and Spot Returns: A Study of the Indian Markets</td>
<td>128-132</td>
</tr>
<tr>
<td><strong>Dipti Ranjan Mohanty and Susanta Kumar Mishra</strong></td>
<td></td>
</tr>
<tr>
<td>Sustaining the Strategic Options and Programmes for the Development of the Nicer Delta Communities</td>
<td>133-136</td>
</tr>
<tr>
<td><strong>G.O. Demaki and P. Okumagba</strong></td>
<td></td>
</tr>
<tr>
<td>How Good are Equity Valuation Models in Predicting Stock Prices?</td>
<td>137-151</td>
</tr>
<tr>
<td><strong>Christoph Hukelmann, Cesario Mateus and Irina Mateus</strong></td>
<td></td>
</tr>
<tr>
<td>Analysis of Sector Indexes: The Case of Logistics</td>
<td>152-160</td>
</tr>
<tr>
<td><strong>Hakan Altin</strong></td>
<td></td>
</tr>
</tbody>
</table>
The Dichotomy between Industrial and Financial Activities and Instability of Capitalism in Veblen's Analysis

Gulenay Bas Dinar

Economic Activity of Oil Price Volatility and Stock Market Behaviour: An Empirical Analysis from Saudi Arabia

Saad A. Alshahrani and Iklaas Gurrib
Abstract

There has been a well-known relationship between macro financial fundamentals and oil prices, yet there is also ample evidence that this relationship weakens during some periods. In this paper, we investigated whether the relationship between oil and macro financial fundamentals vary depending on gold price of oil. To achieve this, a Markov model is implemented to the monthly data for the period 1974 - 2010. In the Markov model utilized in this paper, transition probabilities are endogenous and governed by the volatilities of oil, gold, stock market and exchange rate. This allowed us to endogenously model the switching process. Our results provide evidence that the link between oil price and macro financial fundamentals disappears in the periods of inexpensive gold price of oil. Our findings also provide evidence that the volatilities of the variables matter only when gold price of oil is inexpensive.

Keywords: Oil Price, Gold Oil Ratio, Exchange Rates, Interest Rates, Stock Market Yields, Time Series Analysis, Markov Switching Regimes

JEL Classification Codes: C22, E44, G12

1. Introduction

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