Growth of the private sector and privatization efforts in the developing countries in the world have led to the emergence of various stock markets. Some of these markets are characterized by low volume, insider trading, and syndications. These newly established markets resemble the securities market of the United States in the 1920's before the stock market crash. They lack regulations, and this omission of regulation may be "on purpose", so as not to stifle the newly emerging markets (Filatov (1994); Husted (1994) Rossouw (1994); Ziemba (1994)).

What is the damage caused by insider trading? One potential damage is the public’s perception of financial markets as scams. Perception of unethical trading in the stock markets are one of the biggest stumbling blocks which stop savings flows into the market. When the public lose faith in the stock market and put savings elsewhere, firms cannot raise domestic capital via stock issues.

Insider trading in the stock markets have been of interest to social scientists as well as the legal community. The issue is intriguing, both in terms of ethics and of damages and benefits of insider trading. Economic literature can be used to interpret insider trading from other perspectives. This study argues that the question of insider trading in developing markets can be resolved by the extent stock markets generate externalities and are public goods. It advocates structural changes in the developing markets and examines the conditions under which the Coase Theorem would work.

KEY WORDS: Coase Theorem, economics and law, insider trading, public goods

Growth of the private sector as well as privatization efforts in the developing countries in the world have led to the emergence of various stock markets. Some of which are depicted by insider trading. Law literature uses the arguments of unfairness, breach of fiduciary rights and damage to others to define and rule against insider trading. Economic literature can be used to interpret insider trading from other perspectives. This study argues that the question of insider trading in developing markets can be resolved by the extent stock markets generate externalities and are public goods. It advocates structural changes in the developing markets and examines the conditions under which the Coase Theorem would work.
their trading patterns. Employees who get stock options in their companies are required to file their purchases and sales beforehand, information which is now published by some financial newspapers. This published information on insider purchases and sales of stock are now being used as buy/sell signals by some traders and mutual funds who regard this information as a proxy for the internal health of the firm.

On the average, how much is the rate of return to illegal insider trading? Meulbroek (1992) used Securities and Exchange Commission (SEC) illegal insider trading data for the U.S. equity markets to find that average excess return (above a normal return) to insider trading was around 3% and the price movement of the stock was 40 to 50% of the subsequent price when the “inside” information was announced. She concluded that informed trading helped markets in price discovery earlier than they normally would.

Business literature contains many empirical studies on the impact of insider trading (Leftwich and Verrecchia (1983); Moran (1984); Manove (1989); Bagnoli and Khanna (1992); Noe (1995)). There is no direct discussion in the moral philosophy literature on insider trading. Schools of moral philosophy or principled ethics (cultural relativism, ethical subjectivism, psychological egoism, ethical egoism, rule theory or virtue schools) shed little light on how this issue could be treated under the paradigm of each school, and one doubts that the results would be the same under different paradigms (such as selfish egoism or rule theory). However, one could use a more pluralistic approach and look at the convergence of the above schools rather than their divergence. All schools would agree on the immoral character of deception, injustice, and doing harm. They would also agree that there is a distinction between immoral and illegal acts. Emerging markets in which insider trading is legal could still be judged negatively on moral grounds.

The business literature is usually on the empirical measurement of the occurrence of insider trading, the size of the abnormal profits, if any, and on the price discovery benefit of insider trading information. The sizable literature in law is concerned with the definition and judgement of insider trading cases.

Economics literature can also be used to shed light on how to treat the insider trading issue. Financial markets do generate developmental benefits for the whole economy and economics offers both public and private solutions to cases where social and private costs differ.

In the next section, three main lines of arguments against insider trading as interpreted under contract law are discussed. The next two sections cover how the issue of insider trading could be viewed under economics. The last section gives the conclusions.

**Insider trading in contract law**

Literature has already accumulated on the pros and cons of insider trading under contract law. The opponents of insider trading use three arguments which are those of unfairness, of violation of private property rights (breach of fiduciary rights), and of harm and damage to others. Each of these are briefly summarized below.

**Insider trading and the ‘fairness’ argument**

One of the main ethical arguments against insider trading is that it is “unfair” play since both sides are not privy to the same information. There are two versions of the fairness argument. One version interprets insider information as unequal possession of information and states that insider trading violates the golden rule of treating others as we treat ourselves.

If this version is taken to its extreme, this would imply that all exchange with unequal information is unfair. Yet the judicial system does not interpret all exchanges as such. The system does distinguish between lying/misrepresentation and failure to disclose all. Although it is illegal to misrepresent or lie in an exchange, one need not disclose all information to the other party, and most exchanges are made on unequal information.

Moore (1990) states that insider trading would