

The Research Centre of the School of Economics and Business in cooperation with the  
Bank of Slovenia  
cordially invites you to a research seminar  
on **Wednesday, 4 March, at 13:00 CET in room P-119**  
at the School of Economics and Business

**Ivan Gufler** (University of Bonn)

will present the article:

**Passive investing, diversification risk and financial stability**

**Summary:**

This paper examines how passive investing affects financial stability by altering the composition of equity market risk. Using a valuation-adjusted Bartik instrument, I show that passive ownership causally increases stock return correlations by 3.5 percentage points per standard deviation increase. I decompose diversification benefits and portfolio risk into correlation-driven and idiosyncratic-volatility components using a structural demand system. The analysis reveals opposing effects: passive investing erodes diversification benefits by 3% through increased correlations, while dampening individual stock volatility. The correlation effect dominates—minimum achievable portfolio volatility is 20% higher with passive investors. Overall, passive investing reallocates risk from idiosyncratic to aggregate, non-diversifiable components, reducing the equity market's capacity to absorb shocks. Finally, welfare losses are concentrated among large and well diversified institutions.

**We look forward to welcoming you at the seminar.**