

Understanding Retail Investors: Evidence from China

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Discussion by Darwin Choi



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 - Barber and Odean (2000, 2001, 2008): Retail investors suffer from overconfidence and other behavioral biases
 - Barber, Odean, and Zhu (2009), Kaniel et al. (2012), Kelley and Tetlock (2013), Boehmer et al. (2021): Retail investors correctly predict future returns and trade accordingly
 - Barber et al. (2021), Eaton et al. (2021), Welch (2021): Robinhood investors perform well and engage in attention-induced trading

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- Different subgroups of retail investors behave differently
- Using Chinese data, this paper examines the heterogeneity of retail investors

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- This paper uses data from the Shanghai Stock Exchange
 - Trading and holdings data of 53m retail accounts in 2016–2019
 - Categorized into 5 groups by account balances (RT1–RT5)
 - Also institutional investors (INST) and corporations (CORP)
- Small retail investors (RT1–RT4) negatively predict future returns, but large retail investors (RT5) and INST positively
 - Previous papers mostly treat retail investors as one group
 - Explanations: order flow persistence, liquidity provision, behavioral biases, and information (dis)advantages

#1: The Grouping

To comply with regulatory requirements, all Chinese retail accounts are categorized into five groups by account balances: less than 100,000 CNY (RT1), between 100,000 and 500,000 CNY (RT2), between 500,000 and 3,000,000 CNY (RT3), between 3,000,000 and 10,000,000 CNY (RT4), and greater than 10,000,000 CNY (RT5).

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- **Can the authors provide more information?**
- What exactly are the regulatory requirements? Why 5 groups? How are the cutoffs determined? Do investors know? Are there any differential treatments from the exchange (say, RT5 receive some discount in trading fees)?

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- For investors whose balance is near 10m CNY (cutoff for RT5)
 - Those who performed well in RT4 move up to RT5
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- Retail investors deposit/withdraw money and cross the threshold
 - RT4 deposit/withdraw money and become RT5/RT3
 - Depositing and withdrawing can be a function of past performance/skill

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Dep.var		Ret	Ret	Ret	Ret	Ret
Oib.var		OibRT1	OibRT2	OibRT3	OibRT4	OibRT5
Oib(-1, <u>Persistence</u>)	Estimate	-0.0333***	-0.0279***	-0.0220***	0.0022	0.0063***
	[t-stat]	[-15.84]	[-15.66]	[-12.31]	[0.40]	[6.51]
Oib(-1, <u>Liquidity</u>)	Estimate	-0.0088***	-0.0183***	-0.0212***	-0.0075	-0.0020
	[t-stat]	[-2.61]	[-4.48]	[-3.11]	[-0.82]	[-0.63]
Oib(-1,Overconf)	Estimate	-0.1024***	-0.0407	-0.0658	-0.0151	0.0250
	[t-stat]	[-2.84]	[-0.73]	[-1.09]	[-0.30]	[1.17]
Oib(-1,Gamble)	Estimate	-0.0422	-0.0155	-0.0627*	0.0205	0.0047
	[t-stat]	[-1.49]	[-0.63]	[-1.94]	[0.93]	[0.23]
Oib(-1, <u>Other</u>)	Estimate	-0.0085***	-0.0082***	-0.0058***	-0.0008***	0.0010***
	[t-stat]	[-27.11]	[-24.87]	[-21.68]	[-7.66]	[13.15]
Adj.R2		10.46%	10.32%	10.04%	9.60%	9.51%

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	[t-stat]					
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 - The proxy suggests that RT3 investors are overconfident about their ability in trading Bank of China stock (not in other stocks)
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- Maximum daily returns as a proxy for gambling preferences can be affected by the 10% price limit

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- **Investor Attention**: Baidu Search Index (equivalent to Google Search Volume Index)
- **Disposition Effect**: A proxy for aggregate unrealized capital gains constructed from price and turnover data (Grinblatt and Han, JFE 2005)

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- Do RT5 trade against RT1–RT4 (a wealth transfer)?
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 - For example, psychological and/or institutional frictions cause RT1–RT4 to hold stocks that are difficult to analyze
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- Regress $OibRT5_{i,d}$ on $OibRT1_{i,d} - OibRT4_{i,d}$; negative coefficients suggest that RT5 trade against RT1–RT4

- Very interesting paper and results!
 - Examine the heterogeneity of retail investors using a rich dataset
- I encourage the authors to think more about
 - The regulations regarding the grouping
 - The transition across groups (past performance and deposit/withdrawal)
 - Additional behavioral bias proxies
 - Who are the largest retail investors and why they can outperform