

“Do Behavioral Needs Influence the Trading Activity of Individual Investors?”

(in English)



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Date: 15 November 2010 (Monday)

Time: 4:30pm – 6:00pm

Venue: SO322, Dorothy Y. L. Wong Building

Biography

Dr. Xiaohui Gao holds a BS in Mathematics from Fudan University and a MS in Mathematics from the University of Florida. She received her PhD from the University of Florida. Dr. Gao's primary research interests are in security offerings, including initial public offerings (IPO) and seasoned equity offerings (SEO). She is also interested in the mutual fund industry and has done some research on mutual fund performance and expenses. She recently started to work on behavioral finance topics, including the impact of individual investors' behavioral bias on the stock market.

Abstract

Multiple natural experiments of large jackpot lotteries in Taiwan are used to document a substitution effect between individual investor trading and lottery buying. We establish five key findings. First, when the jackpot exceeds 500 million Taiwan dollars (about 15 million U.S. dollars), the number of shares traded by individual investors decreases by about 7% among stocks with high individual trading fraction, low market capitalization, high past returns, and high past turnover. Second, our approach reveals that the substitution effect is stronger among stocks with lottery features, with a decline in trading of about 9% among stocks with high return volatility and skewness. Third, the magnitude of the documented substitution effect increases monotonically with the jackpot. Fourth, firm-level trading activity reacts negatively to lottery drawings, and is statistically significant for a sizable number of firms. Finally, the aggregate number of shares traded by individual investors declines by 6% with lottery offerings. We attribute the substitution effect exemplified here to behavioral trading needs of individual investors, such as entertainment, sensation seeking, and gambling, and it appears consistent with the wider predictions of behavioral economics and finance.

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