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Investing in What You Know: The Case of Individual Investors and Local Stocks

by Mark Seasholes and Ning Zhu

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Abstract

This paper tests the performance of individuals' equity investments. We study over 40,000 accounts and 950,000 trades from a large discount broker. Individuals invest heavily in local stocks and put 14% more into these stocks than a market-neutral portfolio would suggest. Using holdings-based calendar-time portfolios, we find the local holdings do not generate positive alphas. Using the transactions data, we find local stocks bought actually underperform local stocks sold (though the underperformance is more severe when considering remote stocks). We find no support for the folk wisdom that one should "invest in what you know."

Keywords: <u>Stocks;</u> Local Range; Investment; Equity;

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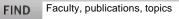
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