

OPTIMISM GONE BAD? PERSISTENT EFFECTS OF TRAUMATIC ECONOMIC EXPERIENCES ON HOUSEHOLDS' INVESTMENT DECISIONS

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BACKGROUND

Personal experiences and investment decisions

- Personal experiences matter for decision making of economic agents
 - Past returns in the financial markets
 - Financial and economic crises
- Will memories fade?
 - "Fading memory" (Malmendier and Nagel, 2011)
 - But not always!

The effect of emotions

- **Emotional tagging:** Brain stores a memory of an event *combined* with an associated emotion
 - Emotions determine the importance of the event
- ⇒ Emotional arousal ↑ → Anchoring in memory ↑



Research question

Can a negative experience in the past have a persistent effect on investment behavior of households today?

A German case study: The Telekom event

- Highly emotional stock market event
- Explain investment behavior of German households today:
 - Low stock market participation rate
 - Knowledge about low interest rates does not matter
- Empirical analysis
 1. Who were affected by the event?
 2. How do they make stock market investment decisions today?

THE TELEKOM EVENT

Chronology of the Telekom shares

- **1996: Deutsche Telekom goes public**
 - Extensive advertisement campaign
 - High media coverage
 - Direct contact to customers
 - Popular among the German population: "People's share (Volksaktie)"

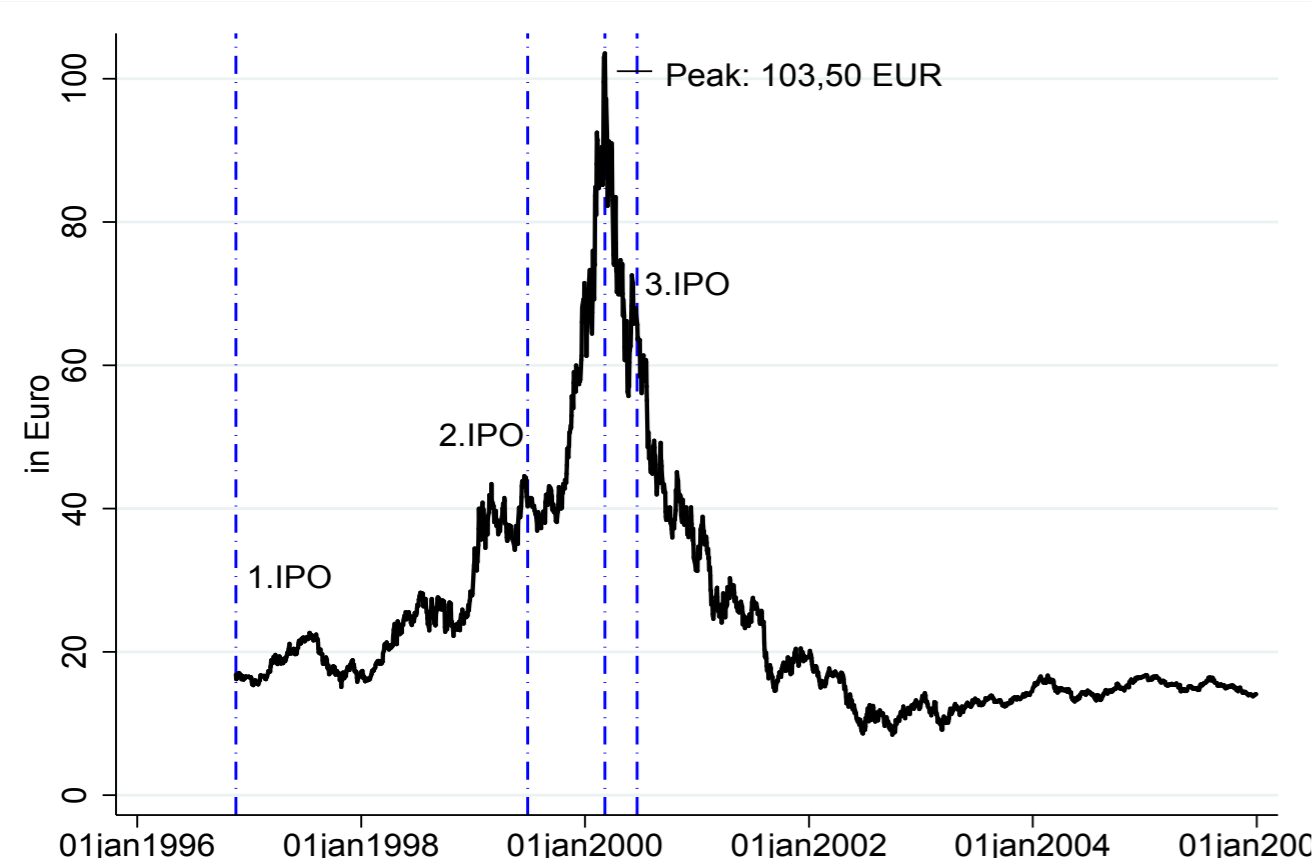
Table 1: Allocation of the IPOs

	DT1	DT2	DT3
Date	Nov 1996	Jun 1999	Jun 2000
Issue	714 mio	281 mio	200 mio
Retail	43%	54%	70%
Instit.	57%	46%	30%

Source: Deutsche Telekom Investor Relations

2000: Fall of the Telekom shares

- Global: Dotcom bubble burst
- Internal: Revealed corruptions of the executive board



Why the Telekom event of all things?

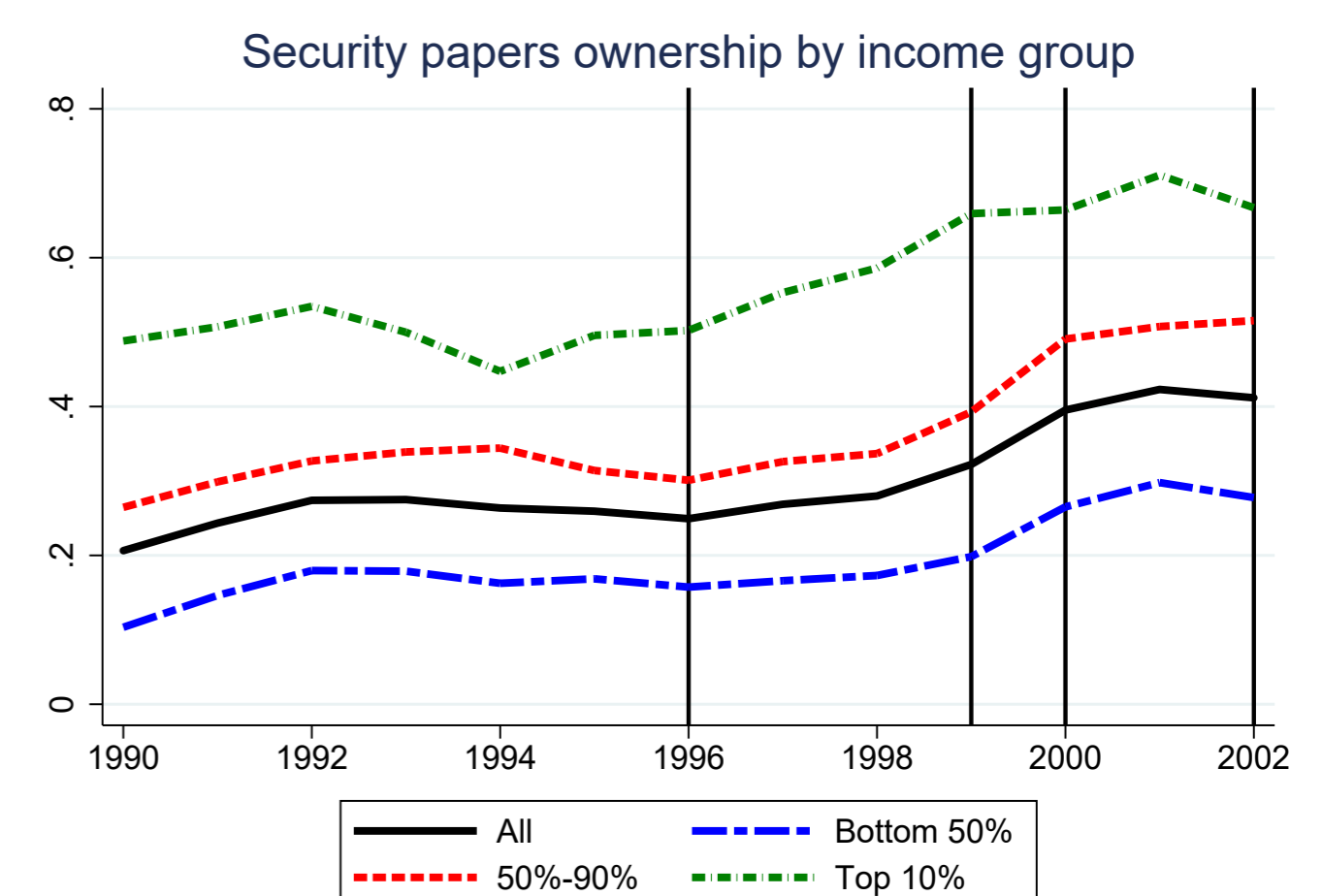
⇒ "Optimism gone bad"

- Mainstream event with high media presence
- High participation rate of unsophisticated investors
- Break in their belief of "safe and high-yield" Telekom shares
- Lawsuits against the executive board

DATA

Socio-economic Panel

- Nationally representative longitudinal study of German households
- Data coverage: Yearly from 1984 to 2017
- Socio-economic characteristics and wealth
- Advantage: Track households over time
- Indication of stock ownership:
 - 1984-2000: Security papers ownership
 - 2001-2017: Stock ownership



THE TELEKOM INVESTORS

Normal investors vs. Telekom investors

- Normal investors: Household heads that regularly invest in security papers (among other stocks)
- Telekom investors: Household heads that entered the security papers market during the three IPOs

Table 2: Summary statistics

	Normal	Telekom
Sex	0.69	0.70
Age	47	43
Married	0.64	0.66
Household size	2.43	2.68
Abitur	0.32	0.19
Former FRG/GDR	0.83	0.76
Income	47588.75	39766.83
Riskless asset	0.97	0.99
Home ownership	0.57	0.48
Risk aversion	4.61	4.93
Fin. risk taking	3.13	2.74
Degree in Economics	0.02	0.00

⇒ Telekom investors more similar to the German average; younger with lower education degree and income

Telekom investors today

Figure: Stock ownership after the Telekom event

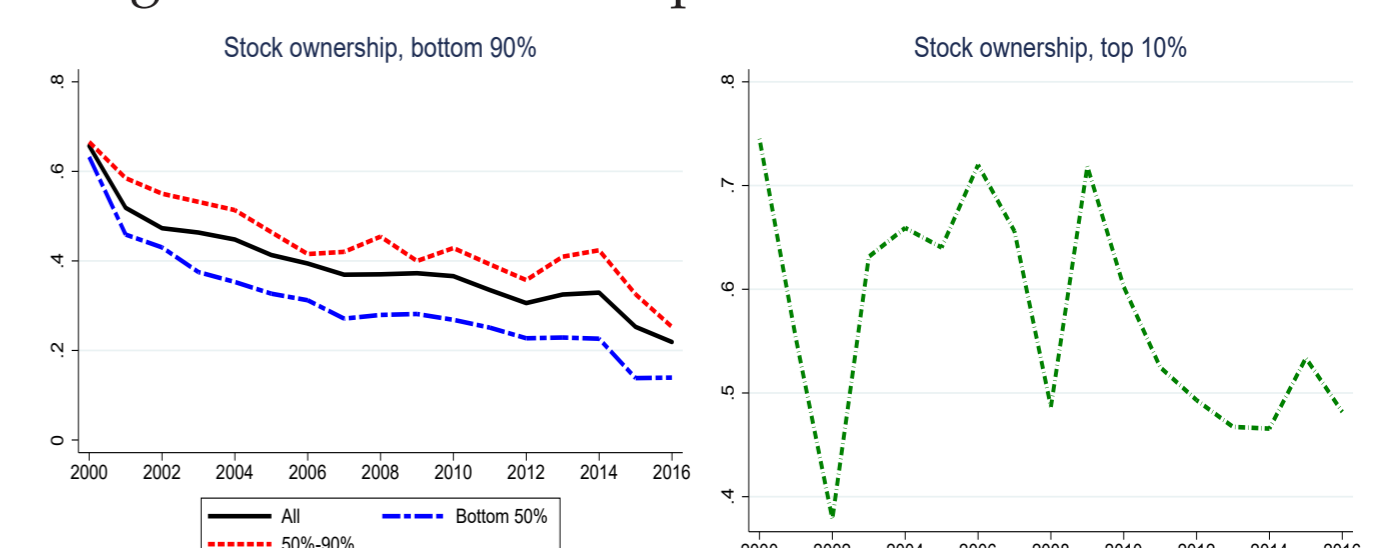


Table 3: Determinants of stock market participation

	Normal	Telekom
Income	0.23***	0.16
Fin. Risk taking	0.13***	0.21***
Past returns	12.6**	43.16
Observations	7358	1120
R ²	0.1	0.17

- Socio-economic variables do not matter for Telekom investors' SMP decisions
- Past asset returns are also irrelevant
- Only financial risk attitude matters for SMP



Conclusion and further steps

Former Telekom investors shape investment decisions differently than normal stock investors

- How strong is the emotional attachment?
 - Sentiment analysis using media coverage
 - SOEP: Survey questions with regard to the Telekom event
- Were these emotions transmitted to the next generation?
 - SOEP: Children of Telekom investors