Trading Narratives

Abstract

We study how investors cognitively represent their investment experience by eliciting open-text narratives about their stock trades in a survey of retail investors and linking them to administrative transaction records. We find that investors disproportionately retrieve stock purchases rather than sales from memory, a pattern largely organized by which positions they still hold. Retrieved purchases and sales are, in turn, represented through systematically different narratives: purchase narratives emphasize company fundamentals and are forward-looking, whereas sale narratives emphasize prices and trading rules and are backward-looking. These representations are not static: as outcomes unfold, investors selectively reconstruct their narratives in ways that justify the original decision. Finally, these representations carry over to beliefs and behavior: which trades investors recall predicts their overconfidence, and their narrative types predict trading styles and the informativeness of their trades. Overall, we show that how experience shapes beliefs and behavior depends not only on what investors experience, but on how they represent it.

This paper is joint work with Katrin Gödker and Cameron Peng.

Christine Laudenbach
Leibniz Institute SAFE/Goethe University Frankfurt