Domestic and Foreign Institutional Investor Behavior in China

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Discussion by:

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Summary

- The authors compare institutional holdings of Qualified Foreign Institutional Investors and domestic institutions in the Chinese stock market
- The results suggest that:
  - Foreign institutions tend to invest in industries where local knowledge is less important, whereas local institutions diversify their holdings more broadly
  - Corporate governance is important only for foreign institutions

General comments

- An interesting and well-motivated topic
- The institutional setting is fairly well described
  - Issues explaining participation in the A-share market could be further explored/explained
    - Most importantly, differences in availability of A and B shares, and enforcement of the ban to invest in both types
    - Is arbitrage possible between ADRs and A-shares?
    - Are A-shares still informationally less efficient?
- How binding are the investment quotas, and do QFIIs vary their investment levels a lot over time?

Literature background

- The paper approaches the topic from a foreign investment viewpoint
- Why not consider literature on institutional holdings more broadly
  - Gompers and Metrick (2001), and numerous subsequent papers
  - E.g. Dahlquist and Robertsson (2001) note that foreign investors in Sweden behave like institutional investors in the U.S.
- Also, Ferreira and Matos (2008) provide findings on institutional investment on a global basis
- Van Niuwerburgh and Veldkamp (2009, 2010) combine info processing choice and portfolio choice – leading to home bias

Specific comments

- Why are dividends not included, given their importance in explaining inst. ownership elsewhere?
- Wouldn’t beta or total risk still be better than operating leverage in measuring firm risk?
  - Use of accounting data also makes assumptions about quality of the data
  - Your operating leverage measure is not independent of financial leverage
  - Would an electric utility be riskier than a software firm?
- Other “missing variables”:
  - Foreign sales, index memberships, foreign listing (e.g. Covirg, et al., 2006)

Specific comments

- What is reported in Table 5?
  - If Panel A reports the number of firms with holdings, what is the E(# firms w/ holdings) in market portfolio?
  - What about # shares in Panel B?
- Does Table 6 report averages for any firms with QFII/Domestic holdings>0?

Specific comments

- Is “partial R^2” a good indicator of variables to be included in your full model?
- How is the dependent variable defined in you regressions?
  - If it is the size of the investment, it is not surprising that size of the firm is positively connected to it
  - Size of the coefficients suggests a scaling problem
  - Should use the % of market cap held by QFII/domestic funds as dep. var.