The Impacts of Institutional Ownership on Stock Returns

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The relation between institutional investors' trading persistence and stock returns is still not clear. Despite the fact that previous studies have demonstrated the persistence of institutional trading can be short-term positively correlated with following stock returns, some empirical studies show that this short-term positive relation holds only under particular circumstances. Recently, Dasgupta, Prat, and Verardo (2011) have even found that the persistence of institutional trading is associated with reversals in stock returns. To fill the gap in the literature, I use a unique monthly institutional ownership data to present new empirical evidence showing that institutional trading not only has a short-term positive impact on stock returns but can also have a long-term negative effect. Moreover, I find that stocks with lower accumulated growth of institutional ownership tend to have greater momentum than stocks with higher such growth. A zero investment strategy of buying stocks with 'LOW'-decile institutional ownership and selling 'HIGH'-decile ones can outperform the market and generate significant abnormal returns.

Key words: institutional investors; herding; momentum effect