Executive Summary

In my thesis I analyze the trading profitability and behavior of retail investors and their dependence on security specific news. I have been endowed with a data set of a German retail broker house, containing daily purchases and sales in several thousand securities which are aggregated over individuals and are recorded during the time span from 2003 to the end of 2011. Furthermore I received a data set from Thomson Reuters, containing firm specific news over the same time span. The news data set additionally includes news tones from which I am able to infer whether news has been positive, neutral or negative for the corresponding firm. My analysis is restricted to stocks. In the first part of the thesis, trading returns of retail investors are determined. Therefore trades are matched via two inventory conventions: Fifo (first-in-first-out) and Lifo (last-in-first-out). After that, monthly realized trading profits are compared to the purchasing cost of stocks to retrieve monthly trading returns. I find solid trading performance with both inventory conventions. On a risk adjusted basis and unadjusted basis, retail investors are able to outperform the risk-free rate and the market index. This somehow astonishing result is however positively biased by a disposition effect – that is the tendency to hold on to losing stocks and to sell winning stocks – which retail investors experience. Furthermore trading returns only explain a minor fraction of the total return compared to e.g. stock price increases. In the second part of the thesis, I analyze whether retail investors experienced an *Attention Bias*. Barber & Odean (2008) showed that individual investors are net purchasers of stocks that grabbed their attention via news for example. In my data set this behavior is confirmed. Furthermore I am able to show that purchases increase the most after negative news and the least after positive news events. This indicates some counter trending trading behavior of individual investors. In the third part of the thesis I combine the first two parts to get insights on whether news and the *Attention Bias* influence retail investors' trading profits. The results show, that positive and neutral news events do not significantly influence trading returns. Negative news events on the other hand significantly reduce trading profits under the Fifo convention. These negative news or the underlying negative event which triggered the news, make stock prices decline, which harms selling prices of stocks already held and consequently impairs trading profitability. In an additional analysis I identify months in which attention based stock purchasing has occurred. After such months, profitability is impaired with results being significant under the Lifo convention. When distinguishing between two time periods, non-crisis (2003-2006) and crisis (2007-2011), I find significant return reductions after attention based purchases in the former. Thus the *Attention Bias* has the potential to hurt individual investors trading profitability.