

The Biggest Issues That Retail Investors Face

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Agenda

- Information Asymmetry/ Exclusive Access
- Gambling in the Market
- Market Manipulation and Fraud
- Low Compliance Cost and Insider Trading
- Lack of Investor Education

Why Are Retail Investors Important?



- They make up about 25% of all investors.
- They are the common people of our nation.
- They continue to rise in the amount of trading volume they hold.

19.5%

OF ALL EQUITY TRADING IN 2020

Information Asymmetry/ Exclusive Access

- Institutional Investor vs Retail Investor
- IPOs
- Resources

	 Retail Investor	 Institutional Investor
Whose money do they invest?	Invest their own money	Invest on behalf of individual investors or shareholders
How much do they invest?	Invests relatively small quantities	Invest & trade in large quantities, such as 10,000 shares or more at a time
How often do they trade?	Trades less frequently managing retirement or as a hobby	Trades frequently & are responsible for most of the trading that happens on the market
How knowledgeable are they?	Non-professional investors with limited knowledge	Specialists with access to exclusive resources & research

Gambling in the Market

- No fees
- Robinhood, Webull
- Treated like gambling



Webull

Market Manipulation and Fraud

- The power of social media
 - Courses
 - TikTok/Reels
- Unethical and false reporting (Bill Ackman)
- Celebrity promotion (FTX, EMAX)

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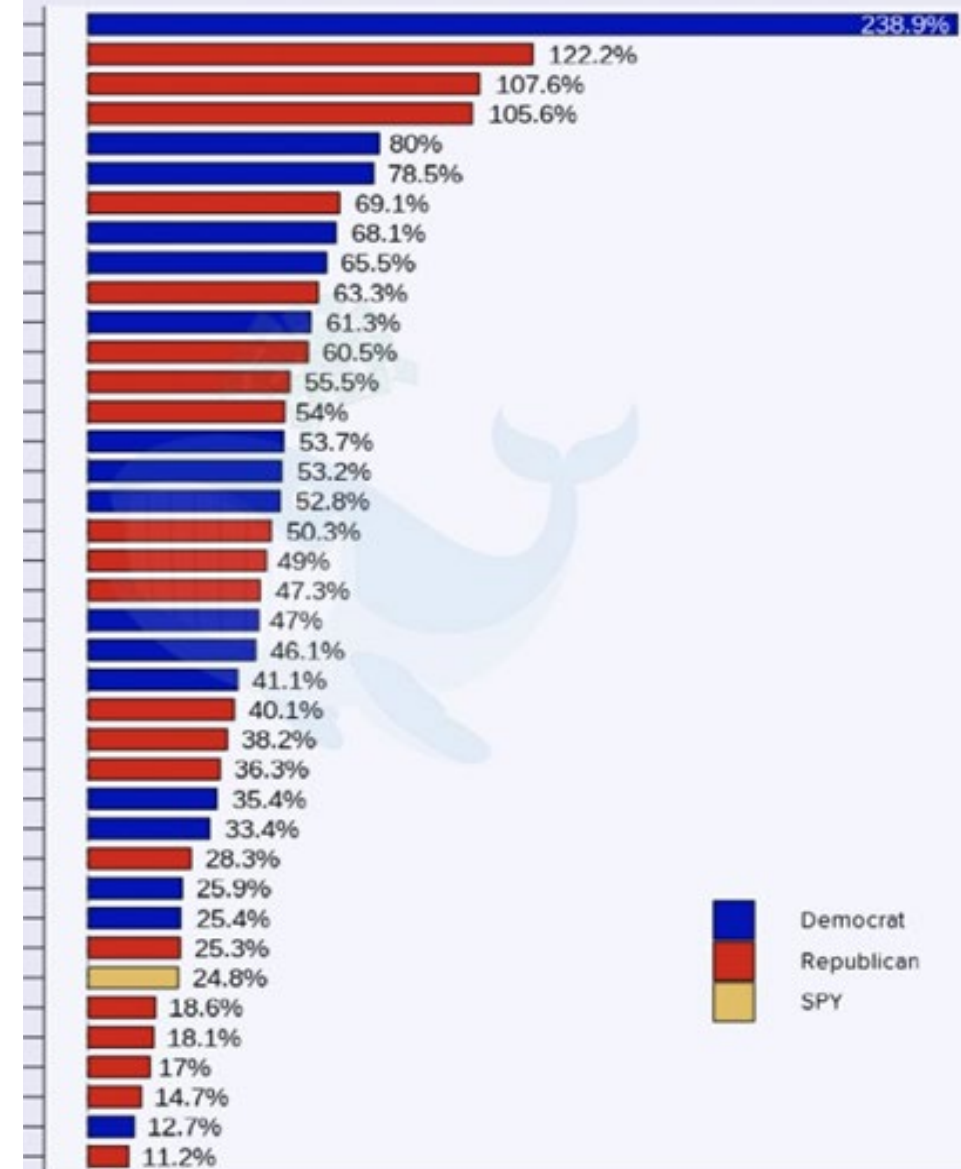
Taken from the Instagram story of @kimkardashian.

Low Compliance Cost and Insider Trading

- Lack of substantial penalty
- Front-running
- Washington DC Hedge Fund

Congress vs SPY in 2023

Returns calculated by estimating current stocks held in each Member's portfolios, then calculating YTD returns. SPY YTD included for comparison.



Lack of Investor Education

- The obvious knowledge gap
- The need for ethical finance professionals
- The job is not finished!

Conclusion

- We must continue to level the playing field between Institutional and Retail investors.
- We must continue to protect investors from fraud and manipulation.
- We must raise the stakes and prevent insider trading across our nation.
- We must continue to educate investors.

Are REITs Real Estate?

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Direct Real Estate Investment

- Real estate is:
 - Immobile
 - Illiquid
 - Privately traded (individually negotiated private contracts)
 - Transactions mostly regulated at the state and local level
 - High transaction costs
- No restriction on investments or strategies
- Tax treatment is based upon the individual investor and the characteristics of the individual property.

(Folger, 2019)

REIT Characteristics

- REITs are:
 - Traded easily in public markets
 - Can also be traded privately
 - Highly liquid
 - Buying and selling regulated by the SEC
 - Low Transaction costs
- REITs receive special tax treatment.

Main Issues?

- REITs are often marketed as a way to ‘invest in real estate’.
 - REIT investors do not face the same search costs as direct real estate investors.
- REITs are easily traded in public markets.
 - Because direct real estate markets are dominated by private contracts, REITs and direct real estate markets will have different volatilities.
 - For example, REIT prices respond more quickly to interest rate movements than direct real estate prices or values.
- REIT payout ratios and income restrictions make them highly dependent on short term credit conditions.
 - Direct real estate investors tend to take out longer fixed rate mortgages on investment properties.
 - REIT prices currently being impacted by debt renegotiations in a higher interest rate environment.

Conclusion

- REITs might be considered real estate because of their structure.
 - Much like holding GM shares would be considered investing in the auto industry, but different.
 - Retail investors may benefit from transparency of public REIT markets.
 - Lower cost of market entry may be an added benefit.
- Retail investors may benefit from transparency in REITs.
 - Can also easily switch between debt and equity REITs.
- The structure of REIT investments ensures products offered to the public are tied to real estate markets.

The Emergence of Retail Investors and Regulatory Response

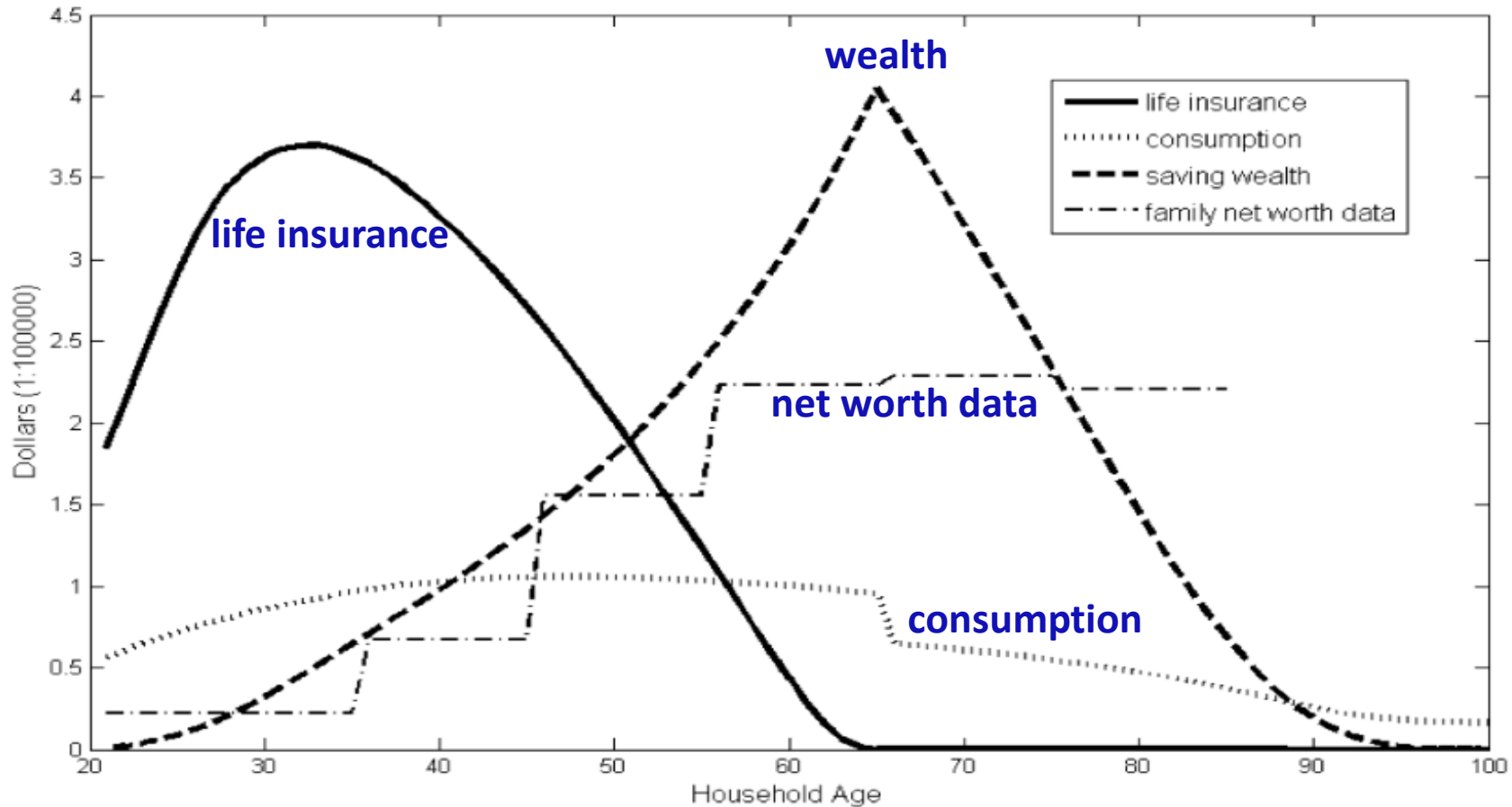
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Optimal Life cycle financial decisions

Wang (2019) developed a heterogeneous-agent life cycle model to generate household optimal life cycle financial decisions with smooth consumption and hump-shaped wealth and life insurance.



SEC Initiatives for Retail Investor Protection

The SEC protects retail investors to ensure the markets function in a fair and orderly manner.

- Regulatory Rulemaking
- Market Oversight
- Disclosure Mandates
- Education Enhancing
- Effective Communications

Enhanced SEC Regulatory Transparency

Significant evidence supports that enhanced regulatory transparency improves enforcement effectiveness and accountability.

- Utilizing the SEC's decision to publicly disclose its comment letters, Hutton et al. (2022) found that regulatory transparency enhances the complementarity of public and private enforcement.
- Guo and Tian (2024) found that publicly disclosing regulators' work output can mitigate moral hazard, increasing regulators' work input and improving their work performance.



Journal of Financial Economics

Supports open access

Journal of Accounting Research

SEC MISSION

- Investor advocate
- Keep pace with evolving models and technologies

19.5%

OF ALL EQUITY
TRADING IN 2020

1.5 BLN.

DAILY INFLOWS IN
2023

KPMG Capital Markets Report

- Completely focused on regulatory environment
- “In addition to continued heavy enforcement, next year we anticipate a **retail-focused** enforcement agenda.”
- “...The most impactful of the proposals under consideration—the order competition proposal”

Regulatory efforts

- 2019 - Regulation Best Interest
- 2020 - Market Infrastructure Rule:
 - National Best Bid and Offer (NBBO) – changes in algorithm
 - Round lot definition changes (*implementation?*)
- 2023 - Reducing transaction execution cycle
- Actions against perpetrators targeting retail investors

Ongoing focus and proposals

- Payment for order flow (*conflict of interest*)
- Exchange rebates (*economies of scale*)
- Access fees
- The order competition

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