ADVERTISING, RISK TOLERANCE AND INVESTOR'S BEHAVIORS: THEORY AND EVIDENCE FROM THE MUTUAL FUND INDUSTRY

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ABSTRACT

This study modifies the risk tolerance parameter in cumulative prospect theory (CPT) as a risk tolerance function of advertising to explain investors' behaviors under uncertainty environment. Our model indicates that advertising would influence investors' redemptions because advertising reduce the speed of CPT investors' diminishing marginal sensitivity to their monetary outcomes when moving away from the reference point. Using mutual fund cash flows data set, this study finds that advertising changes the pattern of existing asymmetric redemption-performance relation, showing that investors are less willing to sell winning funds with high fund family advertising than those with low fund family advertising, and are more reluctant to redeem losing mutual funds with high fund family advertising than those with low fund family advertising.

References available upon request