Insider Trading and Anchoring Bias*

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ABSTRACT

Using a comprehensive insider trading database, we document that US corporate insiders are more likely to sell (buy) as the stock price moves closer to its 52-week high (low). When insiders trade, they buy (sell) disproportionally more as the stock price moves closer to its 52-week low (high). We interpret these findings as supportive evidence that insiders anchor on the 52-week low (high) for purchases (sales). More importantly, we find that the subsequent 60-day stock returns following insider purchases are 3.9 percent higher if such purchases take place when the stock price is far away from its 52-week low than when the stock price is near its 52-week low. In contrast, the subsequent 60-day stock returns following insider sales are 2.5 percent lower for insider sales taking place when the stock price is far away from its 52-week high than when the stock price is near its 52-week high. Our interpretation is that when insiders buy and sell at times when it is suggested otherwise by the anchoring bias, insiders have overcome the anchoring bias because of the private information they have access to. Thus, insider trades that are conducted when the stock price is far away from its anchor levels are more informative. We further show that outsider investors can piggy back on these informative trades and reap economically and statistically significant abnormal returns.

JEL Classification: G11, G14, G15

Key words: Insider trade, anchoring bias, 52-week high and 52-week low, private information

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