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Research on the Characteristics, Development and Decline of Home Bias

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ABSTRACT
This article focuses on studying home bias so that individuals and companies can better reduce home bias, thereby reducing their portfolio risk or improving portfolio returns. The characteristics of companies and individuals, the impact of globalization on the home bias, and whether the use of more general accounting standards can help reduce home bias will be discussed. Through research and comparison, with the development of the times, globalization has indeed reduced home bias to a large extent. However, because of some unchangeable facts, such as the existence of exchange rates, a home bias cannot be eliminated, but it can be used more universally accounting standards to avoid. Perhaps in the future, as the degree of globalization further deepens, and the degree of countries with serious home bias is reduced. Home bias can also be further reduced to increase investor returns while reducing risks.

Keywords: *Home Bias, Globalization, Accounting Standards*

1. INTRODUCTION

The tendency of people to invest in domestic or local stocks or funds is called home bias. This behavior increases the investor's risk to a large extent, because foreign choices are abandoned and the range of choices becomes smaller, and the investment portfolio may not be defined as the optimal investment portfolio. The existence of home bias may be due to the occlusion of information in the past, which made it easier for people to access local information. However, with the progress of globalization, more communication tools appear, and the channels for people to obtain information increase. This development has an impact on the home bias. The impact is inevitable. At the same time, investors should take measures to avoid this behavior to reduce their risks.

This behavior may differ in individuals, such as differences in gender and education level, or differences at the company level, such as the size of the company and the difference in the company's business operations. One section is discussed. In addition, with the emergence of globalization in the second chapter, home bias is indeed weakened, but it has not been eliminated because of the existence of some objective factors. Finally, in Chapter 3, accounting standards are found to affect investors' choices, and the selection of internationally accepted accounting standards can indeed increase investors' confidence in the company.

2. PERSONAL AND CORPORATE CHARACTERISTICS OF HOME BIAS

2.1. Personal characteristics

Whether home bias exists for everyone is a topic that has always been studied. Referring to Lütje and Menkhoff implied that even in an environment where there are no investment restrictions, fund managers will exhibit home bias. Because stock managers believe in information advantages and expect higher returns [1]. However, information advantage usually seems to be just a perceived advantage. Moreover, Lin and Viswanathan wrote the first paper to determine home bias in online financial investment. Home bias is dominated by emotions and psychology to a large extent [2]. Therefore, this emotion and psychology are consistent with the perceived advantage proposed in 2007. In other words, investment bias (including home bias) is caused by genetic factors, which are inherent to everyone.

Even though home bias exists in everyone, there are differences between people. Karlsson and Nordén used multinomial logit models to estimate the likelihood of individuals becoming home bias. First, individuals working in the public sector are more prone to home bias than individuals working in the private sector [3]. More specifically, this may be because stable job choices also indicate a preference for risk, and risk aversion makes unfamiliar foreign securities discarded. Furthermore, a high level of job security (employed in the public sector) will reduce concerns about unemployment, thereby reducing the need for international diversification, and paying more attention to hedging domestic purchasing power. Secondly, from a gender perspective, men are more home bias than women.

2.2. Corporate characteristics

In addition to personal characteristics, home preferences also have specific characteristics at the company level. Coval and Moskowitz identified that information asymmetry may prompt observers to prefer companies that are closely related to them. For example, investors have easier access to information about companies near them, and local companies with relevant information advantages are more favored than remote companies. Local investors can talk to company employees, managers, and suppliers, so important information from local media can be got by them. Additionally, investors may have close personal connections with local executives—all of which may provide them with an information advantage in local stocks [4]. However, compared with the viewpoint of Lütje and Menkhoff, this supposed information advantage is only a perceived benefit. Because fund managers with home bias do not predict stock indexes better than other fund managers and rely less on fundamental analysis. Therefore, "Higher expected returns" have been exposed as permanent "relative optimism" [1].

Based on investing in local companies, investors will also prefer the characteristics of the investment company. As an instance, Coval and Moskowitz suggested that local holdings are usually small non-tradable commodity production companies with high financial leverage. As the times change, this characteristic preference will also change [4]. Ke, Ng, and Wang operate robustness tests to point out extensive evidence of local bias in overseas investment decisions of fund managers. Mutual fund managers prefer U.S. companies with branches in their home countries, even after controlling various company characteristics, including the global visibility and recognition of the company. Moreover, home bias behavior has an unlimited influence on the country, cultural background, and spoken language of fund managers. In addition, the cross-border differences in local presence effects further indicate that in countries with more significant information barriers between foreign companies and local investors, home bias are more prominent [5].

In general, from the analysis of these characteristics, both individuals and companies have home bias, and this behavior is defined as innate. But there is a degree of difference between people, companies, and companies. In other words, the impact of home bias on people and companies can also be changed.

3. THE IMPACT OF GLOBALIZATION ON HOME BIAS

3.1. Globalization reduces home bias

In addition to the personal and company characteristics of home bias, whether globalization will reduce the level of home bias, or the disappearance of home bias is also worthy of attention. In this article, globalization will be interpreted as internationalization. Scholte explained that the term refers to the growth of transactions and interdependence between countries. A more globalized world means a world where more information, money, ideas, investment, goods, and people cross borders between nation-state-territorial units [6]. In other words, globalization has greatly improved the scope and ability of people to obtain information. Therefore, through research and investigation, Riff and Yagil found that globalization significantly reduces home bias. At the same time, in developed countries that have undergone major economic development, social integration is increasing. Interaction takes place every day through tourism, internet connections, cultural product trade. To reduce home bias, the government can encourage interpersonal relationships in the following ways. For instance, reducing restrictions on foreign tourists, encouraging the trade of cultural products, and advocating foreign cultural education in schools [7]. The results show that if the world continues to develop integration and mutual trust between countries in the direction of globalization, home bias will be reduced, leading to a reduction in the cost of home bias and an increase in market efficiency.

However, it is doubtful whether home bias can be eliminated by globalization. The domestic and foreign equity allocation of 38 mutual funds in developed and developing countries has been used by Lau et al. to measure the domestic preferences of domestic investors. Various methods have been used to measure the cost of capital in a country, and all methods have been found to provide conclusive evidence that home bias have a significant economic impact on the cost of capital [8]. Therefore, sufficient evidence shows that even in today's integrated global financial market, the strong preference of domestic investors for domestic stocks not only prevails in countries around the world but also persists. Even if domestic investors from a sample of 38 countries allocate their cross-border equity investments according to the standard portfolio theory, lower capital gains costs and higher risks will be owned by investors.

3.2. Obstacles to globalization

Even if relying on globalization has improved the chances of information being obtained and exchanged, there are still many obstacles to globalization. In the past few decades, many countries have steadily opened their capital markets by relaxing various restrictions on capital inflows and outflows from their stock markets.

However, this liberalization effort has not been so successful in eliminating the local prejudices in various countries. In other words, policymakers, especially countries with greater local tendencies such as China, Brazil, and Thailand, should further promote the free flow of capital to encourage more equity investment outflows. For example, a country can provide investment incentives for domestic funds that invest abroad and provide local investors with more international products for investment. More importantly, they must also convince local investors that international diversification can help reduce the risk of their investment portfolio [8].

At the same time, Levy & Levy mentioned that first, one source of foreign investment disadvantage, namely exchange rate risk, is not expected to disappear. The additional risks implied by the exchange rate cannot be eliminated by hedging. Secondly, as some costs decrease and international diversification increases, this will lead to a further increase in equilibrium correlation [9].

Another limitation of globalization is obvious, politics. The increase in suspicion and separation between the state and the state will bring about economic policy impacts, which may be economic sanctions, public opinion, and home bias may increase again [7].

In summary, globalization does provide more ways for people to obtain information, and policymakers have adopted more tolerant policies to promote world integration. However, there are still countries with large home bias, which requires policymakers to adopt more active open policies. At the same time, due to exchange rate and political factors, even under the influence of globalization, home bias will not be expected to disappear completely.

4. MEASURE TO REDUCE HOME BIAS: THE USE OF ACCOUNTING STANDARDS

4.1. Information cost

Only when the most important influencing factors are discovered can home bias be avoided and thereby reduce the investment risk of investors to attract investment. Ahearne et al. suggest that information cost is an essential factor behind the phenomenon of home bias. To reduce the cost of information, to list or issue public bonds on the US stock exchange, its financial statements must be reviewed by foreign companies that adopt the US generally accepted accounting principles, comply with strict SEC disclosure requirements, and be subject to the strict US regulatory environment. Therefore, significant information costs can be reduced for US investors. At the same time, some evidence suggests that companies from countries with low accounting standards or high transaction costs can improve their prospects among US investors by listing on US exchanges [10]. The way to reduce the cost of information is to use a more transparent system and be subject to strict control, which allows investors to obtain more true company information and thus increase the possibility of their choice. For example, the more common international standards will be easier to understand and more widely used. Section 4.2 will discuss the international common accounting standards.

4.2. IAS and IFRS

International Accounting Standards (IAS) and International Financial Reporting Standards (IFRS) together constitute the main body of current international accounting standards. Listed companies, and sometimes unlisted companies, must use these standards in the financial statements of countries that adopt these standards. At the same time, from 1966 to 2005, several updates were made to adapt to the new era. Therefore, international accounting standards can be considered as part of a legally binding corporate reporting framework that is true and fair [11].

When testing whether companies that voluntarily adopt IAS have different appeals to foreign investors, COVRIG et al. using foreign mutual fund ownership as an indicator of foreign investor preference, foreign mutual fund ownership of companies using IAS are 45% higher than that of companies using local accounting standards, and foreign mutual fund ownership increased by 35% during the year. Therefore, this is strong evidence that companies that adopt IAS have indeed attracted investors to a large extent. In addition, COVRIG et al. also pointed out that foreign mutual fund investments that adopt international accounting standards are concentrated in: (1) Among companies with fewer analysts or lower market capitalizations, companies with poorer information environment consistency use IAS as an additional preparation to attract foreign investors. They can use this behavior to increase their competitive advantage and make up for their relative disadvantages. (2) Compared with local standards, the adoption of IAS has led to a more considerable amount of additional disclosures in various countries. Investors can obtain a large number of company transaction details from disclosures rather than just statements, which is consistent with foreign investors' preference for IAS. Because it reduces the information disadvantages associated with the cross-border investment. In general, the research results are consistent with the hypothesis that the efficiency of capital allocation can be improved by voluntarily adopting international accounting standards to reduce the domestic bias of foreign investors [12].

In addition to COVRIG et al., Khurana & Michas also believes that the United States has a low domestic bias against countries that compulsorily adopt IFRS. At the same time, compared with countries with large differences between IFRS and domestic accounting standards, countries with stricter rule of law and common law sources, and countries with stronger motivation to report high-quality financial information, the reduction of domestic bias in the United States is compelling the adoption of IFRS. After that, it is even more prominent. These results indicate that U.S. investors regard the implementation of standards in countries/regions that enforce IFRS as a critical factor in investing outside the U.S. Overall, the results of the study indicate that a set of universal global accounting standards is critical to the holding of US investors' investment portfolios [13]. This conclusion is also not only for US investors. For global investors, stricter systems have brought more trust and choice.

Finally, as the most important reason for home bias: companies that are abandoned due to high information costs can improve their competitiveness by adopting stricter international accounting standards. For investors, more choices emerge, the so-called information advantage no longer exists, and their portfolio risks will also be reduced.

5. CONCLUSION

This article mainly discusses the personal and company characteristics of home bias, the impact of globalization on it, and the use of IAS and IFRS to improve investor confidence. Through comparison and conclusion, with the deepening of globalization, home bias has indeed weakened, but because of exchange rate and political factors, it is not possible to completely disappear. At the same time, home bias is defined as an inherent characteristic, gender, and job stability will affect the degree of home bias. Finally, companies can use IAS and IFRS to increase investor trust in themselves and reduce home bias.

In the future, due to the continuous expansion of globalization, the increase in ties between countries will inevitably affect individual thinking and concepts. Win-win cooperation should become the mainstream idea, individuals have reduced their investment portfolio risks, and the company has been given a broader stage for promotion. However, due to unknown factors such as politics and inherent genetic problems, home bias should not be expected to disappear completely.

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