

## An analysis of the development of investors in the process of institutionalization

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**Keywords:** Institutional process, Individual investors, Institutional investors

**Abstract:** The regulatory documents of "multi-channel promotion of the effective transformation of household savings into long-term capital in the capital market" and "improvement of the investor structure in the capital market" point out the direction for the development of the capital market in China. In China, the degree of retail investors is high, and the imbalance of financing structure has existed for a long time. In order to reduce market volatility and risk, institutionalization has become an inevitable trend. The process of institutionalization will have a huge impact on both institutional and individual investors. While discussing the inevitability of institutionalization, this paper focuses on the current situation and development direction of institutional investors and individual investors in the process of institutionalization.

### 1. Introduction

On January 3, 2021, the website of CBRC released the guidance of CBRC on promoting the high-quality development of banking and insurance industry. In the opinion, it is emphasized that "banks and insurance institutions should improve the service system suitable for the development of direct financing, provide supporting support for direct financing in various ways, and increase the proportion of direct financing. Give full play to the direct financing function of financial management, insurance, trust and other products, cultivate the concept of value investment and long-term investment, and improve the structure of investors in the capital market. Vigorously develop enterprise annuity, occupational annuity, all kinds of health and endowment insurance businesses, and promote the effective transformation of residents' savings into long-term capital market funds through multiple channels. All kinds of qualified investment institutions are encouraged to participate in the market-oriented and rule of law debt to equity swap."

It reflects the basic national conditions of our country. The direct financing ratio of our country has been hovering below 15%, which is significantly lower than that of developed countries. One of the important reasons is that residents have poor investment consciousness and high saving rate. Due to social culture and living habits, China's savings rate is far higher than the world average. These deposits reduce the efficiency of the fund itself. Compared with direct financing, the participation of banks in indirect financing increases the cost of social financing, reduces the rate of return on loans, and forms potential waste in all aspects. At the same time, too much indirect financing will lead to too much dependence on banks. In the process of financing, banks have affected the stability of the financial system and the capital circulation chain and increased financial risks. And the low direct financing also leads to the financing difficulties of small and medium-sized enterprises. In particular, small and medium-sized enterprises with weak credit ability are more likely to break the capital chain, which is not conducive to the development of emerging innovation industries. In addition, the equity financing scale of about 5% also reflects the imbalance of the development of China's bond and stock market.

Therefore, in order to adjust the unbalanced structure of the high proportion of indirect financing and the low proportion of direct financing and promote the balanced development of China's

financing structure, the capital market must change. We should give full play to the role of banks and insurance institutions in optimizing financing and cultivate institutional investors in the capital market, including the bond market. Strengthen market management ability, strengthen supervision, improve the operation ability and innovative service level of institutional investors, break the restriction of traditional rigid exchange, and cultivate the long-term investment concept of residents. Let the savings of the residential sector enter the capital market through institutional investors. At the same time, we will encourage market-oriented and rule of law debt to equity swap. The market will gradually shift its focus to institutional investors.

In such a trend, both institutional investors and individual investors should make adjustments and changes to adapt to the coming of the institutional era.

## 2. Individual investors in the process of institutionalization

### 2.1 Current situation of individual investors

According to the statistical yearbook of Shanghai Stock Exchange, the proportion of market value held by natural person investors in the total market value has declined year by year, from 23.7% in 2017 to 21.17% in 2018 and 19.62% in 2019. Similarly, there is a big gap between the market value of shares in 2019 and the previous two years. It can be seen that the trend of the institutionalization of China's capital market is also initially emerging, which also meets the regulatory requirements of "multi-channel promotion of the effective conversion of household savings into long-term capital market funds, and improvement of the structure of investors in the capital market". This trend is also one of the necessary ways to develop into a mature capital market.

Different from the low proportion of retail investors in European and American countries, a large number of A-share investors are still working class, and the proportion of shareholding accounts in recent years has been more than 99%. Although the stock market value is still dominated by institutional investors, the excessive number of retail investors also affects the development of the capital market.

And the current economic environment is not friendly to individual investors. Individual investors lack professional theoretical knowledge, have strong speculative trading purpose, and pursue short-term and frequent trading. This kind of operation mode is very speculative, which is not conducive to the maintenance and appreciation of residents' funds, but also easy to expand the risk. On the contrary, institutional investors get far more profits than individual investors with lower trading frequency. At the same time, the fierce competition of Internet financial management and a number of scams also lead to a large number of individual investors losing their lives. In the future, under the influence of policies that favor the development of institutional investors, individual investors will only be more difficult.

Table 1. Share Hold of Investors

	Hold value of natural person investors (100M)	Ratio (%)		
		Natural person investor	General legal person	Professional organization
2019	45506	19.62	64.55	13.92
2018	59445	21.17	61.53	16.13
2017	56662	23.70	60.00	15.58

### 2.2 Suggestions for the development of individual investors

In order to avoid investment risk, people tend to save and bank financial products. Therefore, the financing structure of our country is out of balance. In order to improve the unbalanced structure, stimulate consumption and promote economic growth, the amount of social loans rose sharply. Driven by the rise of bull market and real estate industry, residents' stock speculation and housing hoarding have become a new way to attract funds. But this highly speculative and fanatical

investment model leads to increased market instability, which can only temporarily stimulate economic growth, not the long-term way.

For long-term development, the market needs to take a more moderate path. Institutional investors are far more professional than individual investors, so the investment risk of institutional investors is smaller, and the return and risk of capital market will be relatively more balanced. Therefore, for the stable residential sector, institutional investors are the medium or better choice. Residents entrust institutional investors to invest and purchase financial products. Institutional investors absorb the scattered funds of retail investors to form a stable capital supply. Both sides have a positive effect, which not only enlarges the scale of institutional investors, strengthens their strength, but also ensures the stability of the fund income of retail investors.

One of the reasons why Chinese residents can't participate in direct financing is that the pension savings system is not perfect. Individual investors should also actively cooperate with national policies to transfer some financial assets to private pension savings. In the future, the residential sector will participate in direct financing in the form of annuity, occupational annuity and personal pension insurance.

To improve the competitiveness of China's capital market, individual investors should change their investment style and actively adapt to the era of institutionalization. Actively cooperate with the establishment of multi-level pension system, rely on institutional investors for financial management, and reduce the blindness caused by private investment.

### **3. Institutional investors in the process of institutionalization**

#### **3.1 Current situation of institutional investors**

According to the statistical yearbook of Shanghai Stock Exchange, the proportion of institutional investors' stock market value in the total market value has increased year by year. The proportion of general legal persons' stock market value has increased from 60% in 2017 to 64.55% in 2019. The proportion of professional institutions' stock market value has increased from 15.58% in 2017 to 16.13% in 2018. The overall institutional investors have increased by 2.89%. The overall environment of A-share has changed, the implementation of the new securities law and the promotion of the comprehensive registration system have changed the investor structure of the capital market. The proportion of institutional investors increased while that of individual investors decreased.

This kind of structural change is also the necessity of market development, and the law of market evolution is the transition from individual investors to institutional investors. Institutional investors have more knowledge reserves, more advanced theoretical system, and more transparent market information. The stable investment mode of institutional investors is more in line with the current market and social and economic needs. Instead of blindly pursuing volatility, it is the performance of mature markets to focus on performance growth.

Although institutional investors are more professional and stable, there are some disadvantages.

First of all, the contribution of retail investors to market activity is higher, which means that the market liquidity is better. If the proportion of investment bank investors is large, it may reduce the market trading frequency and trading volume. Secondly, the service level of investment institutions in China needs to be improved, the innovation ability of investment banks is insufficient, and the degree of product homogeneity is serious. The selection scope of residents is small, and the project is not attractive to residents. The supervision of institutions is not strong enough, and there is no credibility for the public. In contrast, the public will still have the deposit or bank financial products with the nature of rigid payment. The degree of information openness and transparency of institutions is small, and the investment risk of residents is large. All of these problems will make it difficult for institutional investors to absorb public funds, so they cannot expand the scale of institutional and market investment.

Moreover, although the return rate of institutional investors is rising, the overall scale of the industry is still a short board. As far as the scale of investment banks is concerned, there is still a gap

between the total scale of investment banks in China and that in mature markets in Europe and the United States.

### **3.2 Suggestions on the development of institutional investors**

Facing the situation that the degree of retail is too high in our country, the realization of the institutional era needs many changes from the government and institutional investors. First of all, in order to attract more residents' funds, institutional investors should open more investment channels, innovate financial products, improve the differences between products and projects, and improve and stabilize the rate of return. Institutional investors should make full use of their own advantages and operate more rational investment strategies. Only when the product income of institutional investors is considerable, will it have enough attraction to make individual investors give up speculation and residents give up saving.

Institutional investors should also establish an industrial and integrated monitoring system, with information symmetry between institutions and clients, and enhance mutual trust. A perfect supervision system is one of the keys to establish a long-term investment channel. Only when residents rely more on institutional investors, can they effectively play the direct financing function of financial management, insurance, trust and other products, and optimize the investment style of the stock market.

At the same time, financial institutions should also focus on the independent development of private pension products, and play the second and third pillars of pension. Institutional investors should make full use of private pension and public fund. Institutional investors should open the way for pension to enter the market, guide the residents to turn their savings into private pension, and change the direction of family financial management. Institutional investors should gradually focus on the development of public funds, pensions, insurance funds and foreign capital, promote the process of institutionalization, guide the flow of retail funds, and catalyse the scale effect of funds.

## **4. Summary**

Reducing the proportion of retail investors and enhancing the strength of institutional investors is one of the mature performances of the capital market. The imbalance between direct financing and indirect financing will also be improved in the process of institutionalization. The institutionalization process can improve the frequent fluctuation, strong speculative atmosphere and blindness brought by the high degree of retail investors.

In the process of institutionalization, both institutional investors and individual investors should make changes to adapt to the environment. In the increasingly weak environment, individual investors should withdraw in time, choose reliable institutional investors and invest rationally. At the same time, we should actively invest in private pension savings in line with the policy. Institutional investors should improve their own strength, attract individual investors to improve the regulatory system and expand the industry scale. We should make full use of private pensions and public funds. The process of institutionalization is the development of capital market, in which investors need to adjust their investment style and strategy in time to obtain income and form a positive cycle with the market.

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