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Institutional Investors and Equity Prices

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Abstract

This paper analyzes institutional investors' demand for stock characteristics and the implications of this demand for stock prices and returns. We find that “large” institutional investors nearly doubled their share of the stock market from 1980 to 1996. Overall, this compositional shift tends to

increase demand for the stock of large companies and decrease demand for the stock of small companies. The compositional shift can, by itself, account for a nearly 50 percent increase in the price of large-company stock relative to small-company stock and can explain part of the disappearance of the historical small-company stock premium.

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