Imitation-related performance outcomes in social trading: A configurational approach☆

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ABSTRACT

This paper draws on the resource-based view and risk-related research to examine imitation-related configurations that explain performance outcomes in social trading. The study applies qualitative comparative analysis to examine 16,964 investment observations at eToro, the world's largest social trading platform. The results show that the experience and the imitation of traders, in combination with a low risk level, equifinally explain similar performance outcomes. The findings contribute to the literature on social trading and the resource-based view by exploring imitation as a valuable strategy, conceptualizing and empirically validating the role of risk in social trading, and drawing on qualitative comparative analysis to develop a more complex configurational understanding of the examined phenomenon.

1. Introduction

Scholars and investors devote an increasing amount of attention to social trading. In social trading, investors manage their portfolio in online communities that offer specialized tools and methods for making financial investments. The nascent literature on social trading (e.g., Oehler, Horn, & Wendt, 2016; Pentland, 2013; Wohlgemuth, Berger, & Wenzel, 2016) explores the unique features of this emergent but promising form of investing that other streams of literature do not fully illuminate. One of these features is *copy-trading*, a functionality of social trading platforms that allows investors to "automatically, simultaneously, and unconditionally replicate other investors' trades" (Wohlgemuth et al., 2016, p. 4970). This feature promises inexperienced investors with below-average trading performance to improve their performance in financial markets by imitating the investment decisions of more experienced investors (Pentland, 2013). Prior research highlights copy-trading as a key feature of social trading (Wohlgemuth et al., 2016). However, the literature on this phenomenon does not fully illuminate the performance outcomes of imitation-related configurations in social trading. This paper addresses this gap by drawing on the resource-based view (e.g., Barney, 1991; Peteraf, 1993) and risk-related research (e.g., Berger & Fieberg, 2016; Markowitz, 1952) to examine the following research question: *Which imitation-related configurations explain performance outcomes in social trading*?

For this purpose, the present paper uses qualitative comparative analysis (QCA) to analyze 16,964 investment observations at *eToro*, the largest social trading platform worldwide. The results show that the experience of traders and their imitation, in combination with similar risk preferences, equifinally explain similar performance outcomes. These findings contribute to social trading research (e.g., Oehler et al., 2016; Wohlgemuth et al., 2016) through an in-depth examination of the imitation-related configurations that explain performance outcomes in social trading. Furthermore, the study complements work on the resource-based view focusing primarily on the barriers to imitation (e.g., Jonsson & Regnér, 2009; Madhok, Li, & Priem, 2010), by examining the performance outcomes of configurations that relate to the *doing* of imitation. In addition, the study complements the few works that draw on configurational approaches to examine resource-based phenomena (e.g., Hervas-Oliver, Sempere-Ripoll, & Arribas, 2016; Ho, Plewa, & Lu, 2016; Lisboa, Skarmeas, & Saridakis, 2016) by using QCA to develop a more complex understanding of the performance outcomes of imitation-related configurations.

2. Social trading and imitation

Social trading is an aspect of what is termed *fintech*, that is, the recent emergence of digital technology in financial services (Chishti & Barberis, 2016). Social trading is a way of making trades through specialized, investor-focused online communities (Wohlgemuth et al., 2016). All members of the trading community have access to the trading decisions that investors make on the platform. In addition, traders can communicate the strategies underpinning their investment decisions, exchange information, and follow other traders and their investment decisions (Oehler et al., 2016; Wohlgemuth et al., 2016).

Social trading is different from other forms of financial trading in that social trading platforms facilitate copy-trading: the simultaneous and unconditional imitation of other investors' trades through automatic brokerage execution (Wohlgemuth et al., 2016). This feature enables investors on social trading platforms to benefit from the wisdom of exceptionally successful traders or the "wisdom of the crowd" (Pan, Altshuler, & Pentland, 2012, p. 203). Accordingly, typical transaction costs, such as for gathering information on investment alternatives or portfolio selection (Markowitz, 1952), are accrued by the followed trader, but not the follower. Therefore, social trading is very attractive for less experienced traders: the technical ability to directly imitate the investment decisions of experienced traders promises "average traders—who are often losers in the financial markets [to turn] into winners" (Pentland, 2013, p. 7). Nevertheless, while prior research acknowledges imitation through copy-trading as a unique opportunity and *the* most important feature of social trading (Wohlgemuth et al., 2016), previous studies pay little empirical attention to the performance outcomes of imitation-related configurations in social trading (Oehler et al., 2016).

To gain a better understanding of the performance outcomes of imitation-related configurations in social trading, this paper now turns to the resource-based view, a stream of literature in which imitation is an important topic.

3. Resource-based view and imitation

The resource-based view (Barney, 1991; Peteraf, 1993; Wernerfelt, 1984), also called resource-based theory (Barney, Ketchen, & Wright, 2011), is a theoretical approach in the management literature that considers firms as bundles of resources. Resource-based studies typically define resources as any and all kinds of assets, capabilities, processes, information, attributes (Barney, 1991), or alternative stocks of available factors that actors own or control (Amit & Schoemaker, 1993). Departing from theories that attribute the origin of differences in firm performance to attractive markets (e.g., Porter, 1980), the resource-based view states that firm heterogeneity is the underlying reason for differences in performance and the key cause of enterprises achieving a competitive advantage (Barney, 1991; Peteraf, 1993; Rumelt, 1991). The resource-based view explains such heterogeneity by arguing that firms possess different resources. More specifically, the resource-based view suggests that, to generate above-average returns, firms must possess resources that are valuable, rare, inimitable, and non-substitutable (Barney, 1991). According to the resource-based view, imitation plays a key role in explaining performance outcomes: if competitors are able to imitate a resource, they "hurt a given firm's performance" (De Carolis, 2003, p. 28) because this resource becomes incapable of generating uniquely above-average returns but delivers average returns at best, given that several firms use the same resource to create the same value (Kraajenbrink, Spender, & Groen, 2010). Owing to this important role of emulation processes in explaining performance outcomes, imitation is the "lynchpin of resource-based theory" (King & Zeithaml, 2001, p. 75).

Prior research primarily focuses on exploring barriers to imitation through which firms sustain above-average returns (Dierickx & Cool, 1989; Lippman & Rumelt, 1982). Most works highlight a potential imitator's *inability* as a key barrier to imitation (Madhok et al., 2010). For example, King and Zeithaml (2001) argue that the complex embeddedness of resources in firms prevents potential imitators from understanding how these resources generate above-average returns. Similarly, Thomke and Kuemmerle (2002) show that potential imitators are less able to emulate resources the more these resources are interconnected with other resources. In turn, Grahovac and Miller (2009) identify costs of imitation as a central barrier to imitation; they show that the costs at which potential imitators are able to emulate another firm's resources may be higher than expected benefits and, therefore, prevent imitation. More recent works consider the *unwillingness* of imitators a key barrier to imitation (Jonsson & Regnér, 2009; Madhok et al., 2010). For example, Jonsson and Regnér (2009) show that potential imitators may be unwilling to imitate because of institutionalized norms, such as professional codes, that prevent them from doing so. In turn, Madhok et al. (2010) show that potential imitators may be unwilling to imitate because they may have alternatives available that are more profitable than emulation.

While these studies provide insightful contributions to a better understanding of barriers to imitation that help firms with above-average returns sustain their competitive advantage, few studies examine the performance outcomes of imitation (De Carolis, 2003; Ethiraj & Zhu, 2008; Pacheco-de-Almeida & Zemsky, 2012; Posen, Lee, & Yi, 2012). An examination of imitation-related configurations that explain performance outcomes is particularly interesting in the context of social trading: the technological affordances of social trading platforms enable traders to imitate the decisions of other investors (Wohlgemuth et al., 2016) and attract inexperienced investors in particular, who aim to make more profitable trading decisions (Pentland, 2013). Accordingly, social trading platforms undermine the inability and unwillingness to emulate others' valuable resources as classical barriers to imitation, and render the examination of configurations that explain the performance outcomes accessible. Therefore, this paper builds on the resource-based view to examine configurations that explain performance outcomes in social trading.

4. A resource-based view on performance outcomes of imitation-related configurations in social trading

The resource-based view suggests that to generate above-average returns investors must accumulate valuable resources. This insight stems from the assumption that investors cannot freely purchase value-generating resources in factor markets but must develop and accumulate them over time through gaining *experience* (Barney, 1986, 1991; see also Priem & Butler, 2001a, 2001b). However, as the resource-based view outlines, resources will no longer yield above-average returns if others imitate them; instead, they generate *average returns* at best, given that others can draw on the same resources to create the same value (Kraajenbrink et al., 2010). Accordingly, from a resource-based perspective, experience in social trading is a key condition for explaining above-average returns on social trading platforms. To generate above-average returns, investors must accumulate a competence in social trading by accumulating experience in conducting investments on social trading platforms over time.

In turn, the resource-based view suggests that imitators are unable to generate above-average returns. This idea originates from the assumption that imitators cannot exceed the performance of those firms that they imitate; therefore, by imitating, investors can only achieve competitive parity at best (Madhok et al., 2010). However, especially inexperienced traders use the copy-trading functionality of social trading platforms (Pentland, 2013). As prior research suggests, these traders generate below-average returns if they make independent investment decisions; by relying on the copy-trading functionality, unskilled investors may offset their lack of experience in social trading by *imitating* the decisions of experienced investors (Pentland, 2013) and, thus, achieve similar (*average*) *returns*. Therefore, for inexperienced