Partisanship in Mutual Fund Portfolios: Biased Expectations or In-Group Favoritism?
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Motivation
- Rise in political polarization in the US society
- Does political alignment affect economic expectations and create in-group favoritism?
- Past literature documents economic expectation bias for credit rating analysts, bankers and company management
- There is also evidence regarding in-group favoritism for mutual funds, news networks and company boards.
- This paper examines these two channels for mutual fund managers

Main Results
- Misaligned managers have a pessimistic outlook: they underweight small-cap, volatile and value stocks and overweight momentum stocks
- Republican managers increased portfolio beta significantly after the 2016 Trump election
- There is no evidence for in-group favoritism once managers without affiliation are removed from the sample
- There is a partisan bias in holdings of stocks exposed to COVID-19 but limited evidence for past pandemics (H1N1, Ebola and Zika)
- There is also a partisan bias in Brexit-exposed stocks affirming that the bias manifests in politicized topics

Economic Expectations
To test the "biased economic expectations" hypothesis, I use the following regression model on the sample of only the "donating" managers:

weight_\text{p} = \alpha + \beta_1 \text{misalign} \times \text{variable}_i + \Gamma \text{Controls} + \delta_1 + \lambda_\text{side} + \psi \text{donation} + \varepsilon

- \text{weight}_p \text{ is the portfolio weight of stock } j \text{ in fund } i \text{ in month } t
- \text{misalign} \text{ indicates the manager is not aligned with the incumbent party}
- \text{variables}_i \in \{ \text{bm}, \log(\text{mkt. cap}), \text{idio. vol.}, \text{12-mth ret}, \text{beta} \} \equiv \Gamma \text{ Controls}
- \delta_1, \lambda_\text{side} \text{ and } \psi \text{ are fund-month, industry-month and state-month FE}
- Standard errors are triple-clustered by fund, by stock and by month

Data & Sample
- Following Hong and Kostovetsky (2012), I construct a sample of U.S.-based active, equity mutual funds with a single manager
- 1,627 managers and 2,139 funds for 01/2005 to 06/2020, while HK find 2,362 single managers for 1992 to 2006
- A Morningstar-CRSP linktable is used to obtain holdings data from CRSP
- Using FEC data, the final holdings data has donation data for 332/1,341 managers (25%)
- Measure of a stock’s exposure to a pandemic is from Hassan et al (2020)

Economic Expectations
\begin{align*}
\text{Economic Expectations} \\
\text{In-Group Favoritism} \\
\text{Partisan Bias & Pandemics}
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