

# Financial econometrics

Business



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## Fund Manager Allocation Fund Manager Allocation Strengths of the Study

Highly skilled fund managers can exploit market inefficiency better.

The basic idea is that fund families allocate more highly skilled managers to less efficient market segments since skill pays off more in these segments.

### Weaknesses

In markets that are more efficient active management does not pay off; hence, investors should buy index funds rather than actively managed funds.

A higher return predictability suggests lower efficiency in the high yield segment than the investment grade market.

### Assumptions

Skilled Managers are rewarded more in less efficient markets

Fund families allocate more highly skilled managers to less efficient market segments.

### Robustness Test

#### GMAT as alternative skill measure

The Graduate Management Admission Test (GMAT) scores are used instead of SAT scores to capture manager skill in measuring alternative skill.

It is worth noting that the alternative skill measures are based on SAT score

The same element or understanding is used to calculate the three alternative ways to estimate the managers' skill including SAT percentile in mathematics, SAT percentile in critical reading, and SAT percentile in critical reading (Fang, Alexander, and Monika, 2014; Pg. 662).

### Alternative performance metrics

To test the robustness or effectiveness of our results with respect to the factor models we have chosen.

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## Temporal stability

The sample is split into two parts

### Proxies Chosen

#### 1. High Yield Segments

HY fund managers have attended business schools with slightly higher matriculates SAT scores. Almost half of the managers hold an MBA degree, and about 25% hold a CFA degree but are less experienced. It should be noted that the HY managers yield higher gross returns.

#### 2. Investment Grade Segments

The proportion of index funds is much higher at 18% in the IG segment than in the HY segment with only 2%. This observation supports the claim that the IG segment is more efficient than the HY segment.

### Main Assumptions of the Study

Our basic idea is that fund families allocate more highly skilled managers to less efficient market segments.

Skill is rewarded more in the less efficient HY market segment than in the more efficient IG segment.

### Selection Bias

The Possible selection bias in this study may be the restriction of our sample to managers with an MBA degree.

### Identification Strategy

The main strategy used to identify the managers as investment grade and high yield is based on skill and focuses on the following:

Holders of master's in Business Administration

Non holders of Masters in Business Administration

Holders of Certified Financial Analysts

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## Other Qualifications

### Experience in the field

### Endogeneity Problem

The fund family has to decide how to assign the managers to two funds: operating in the inefficient market segment and operating in the more efficient segment. To maximize its profit, the fund family allocates managers to funds so that overall fund performance is maximized (Fang, Alexander, and Monika, 2014; Pg. 667). The rationale is that fund performance determines fund growth, given the industries fee structure, fee income, and profit at the fund family level. Since the skill fund family to assign more highly skilled manager to the less efficient market segment, and the less skilled manager to more efficient segment.

## References

FANG, J., ALEXANDER, K. & MONIKA, T. (2014). Fund Manager Allocation. *Journal of Financial Economics*. 111, Pp. 661–674. NY: Elsevier Publishers.