

DISCUSSION OF “THE ECONOMICS OF MUTUAL FUND MARKETING”

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Summary

- Research Question: how does **marketing** decision shape mutual fund companies' performance and future growth?
- Strategic marketing employment policy
 - **Learning**: lower investors' participation cost
 - **Signaling**: change investors' beliefs about the managerial skill → **persistence** of marketing strategy

Skill	Low Past Performance	High Past Performance
Low	/	MKT
High	MKT (signaling)	MKT

Summary

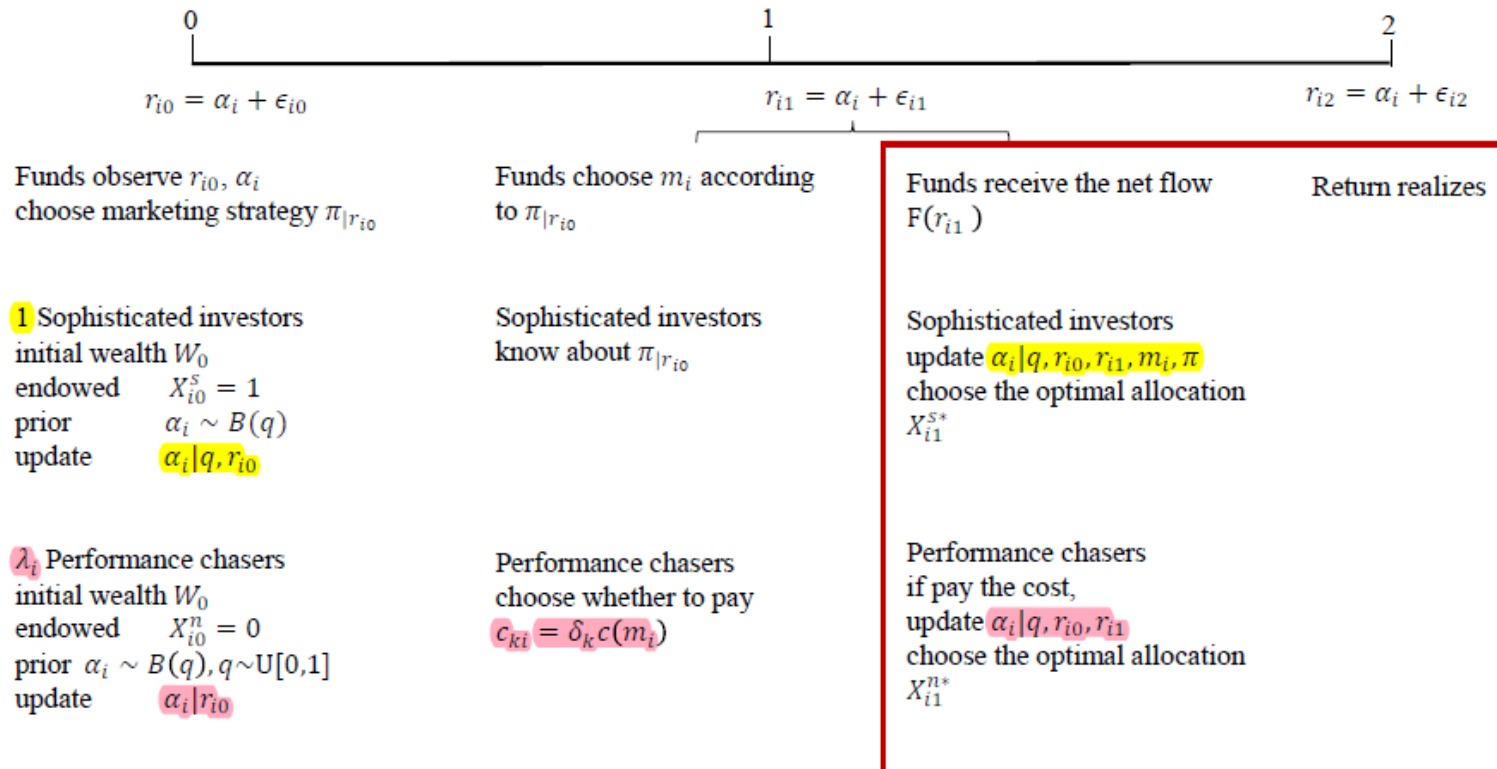
- Key Predictions:
 - High-type fund companies adopt more **persistent** marketing strategies.
 - The **level** of marketing effort is positively correlated with fund company size and fund flows.
- Empirical Strategy and Findings: a novel labor-based measure, marketing employment share

	Performance	Assets, Flow, Growth
Vol(MKT)	-	/
MKT	/	+

Comments

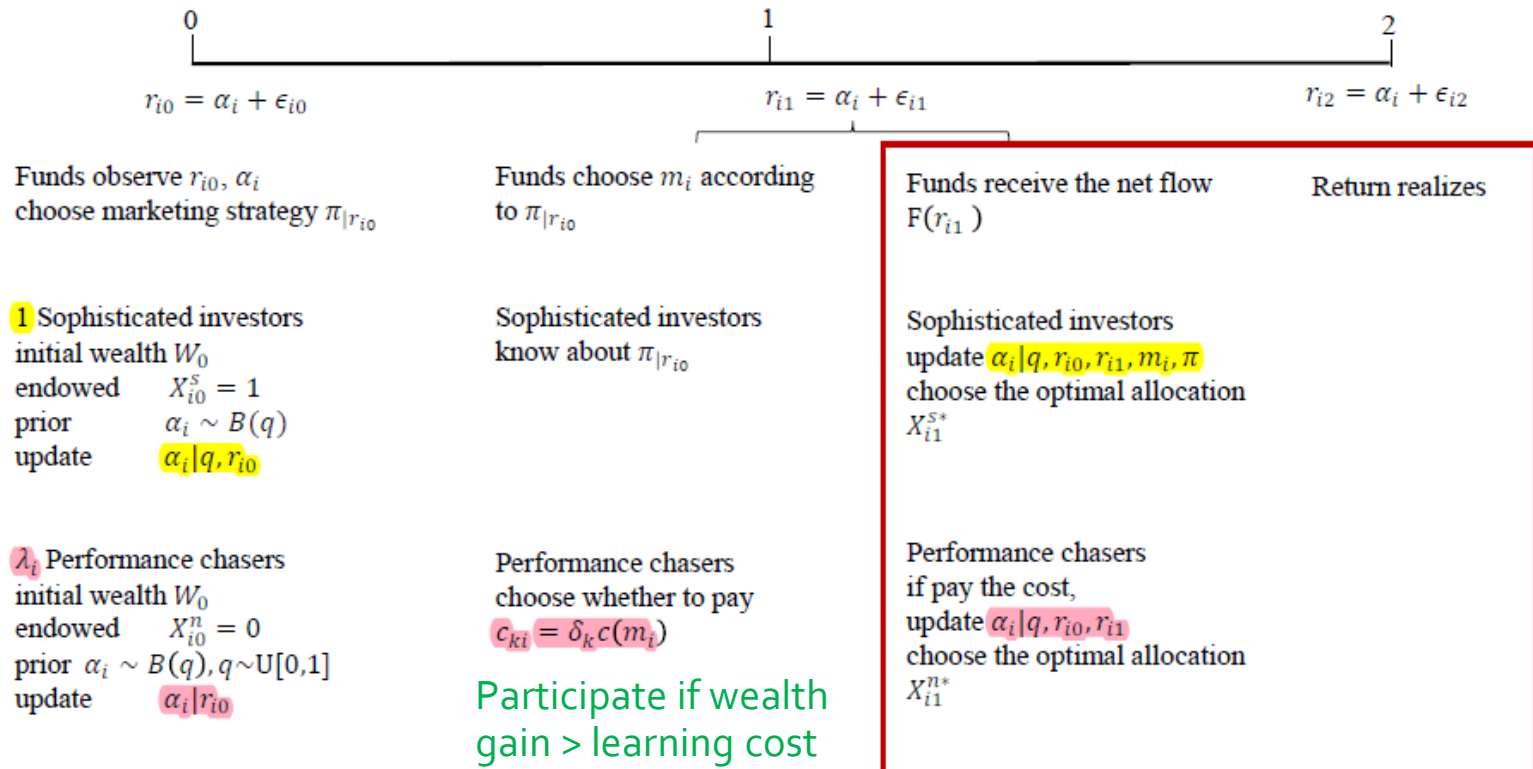
- Great paper on an important topic that needs more theory
- A rich set of predictions and results, novel insights
- My discussion:
 - Model setup
 - Managerial skill
 - Other testable predictions and extensions

Model Setup



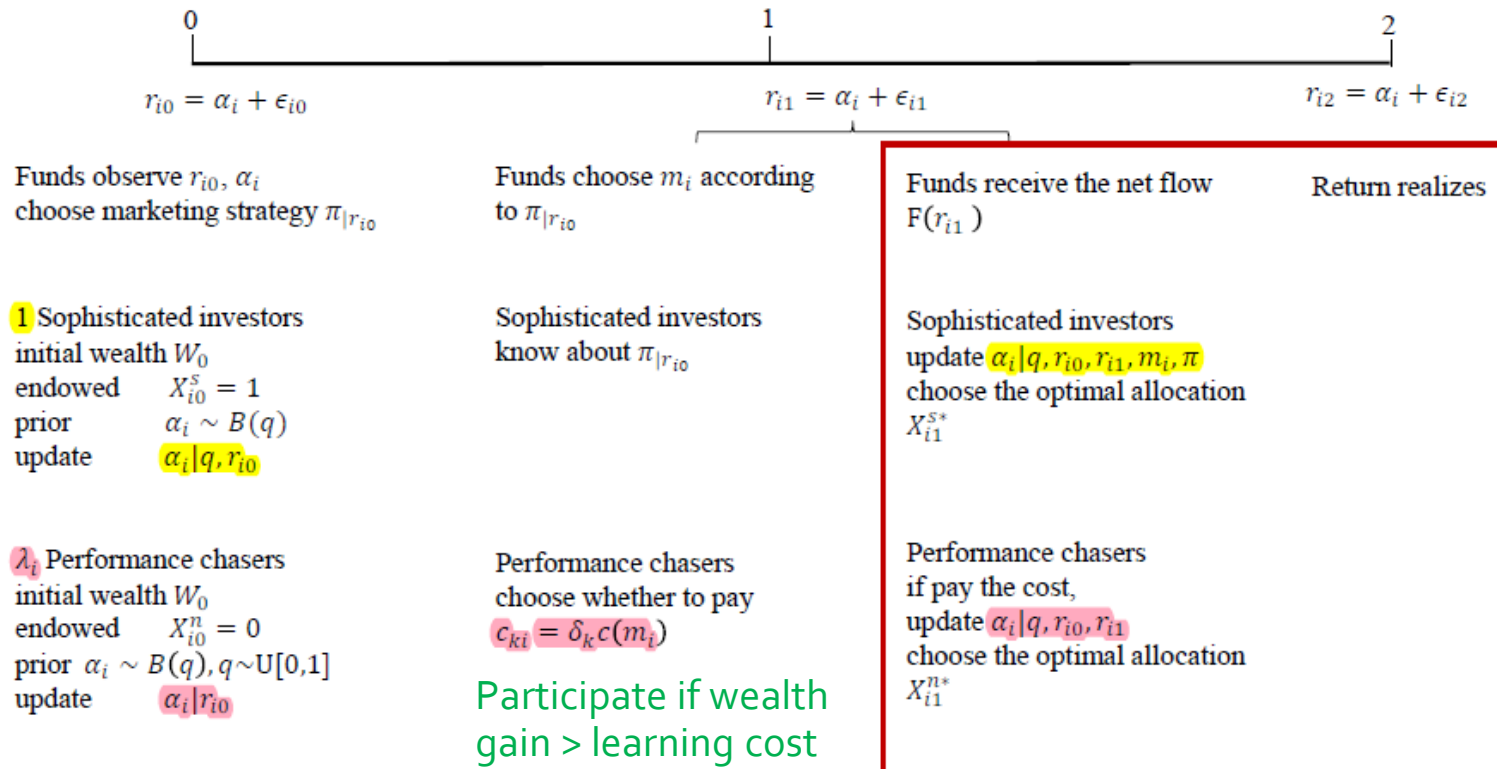
- The potential pool of performance chasers (λ_i) could be a function of marketing strategy.

Model Setup



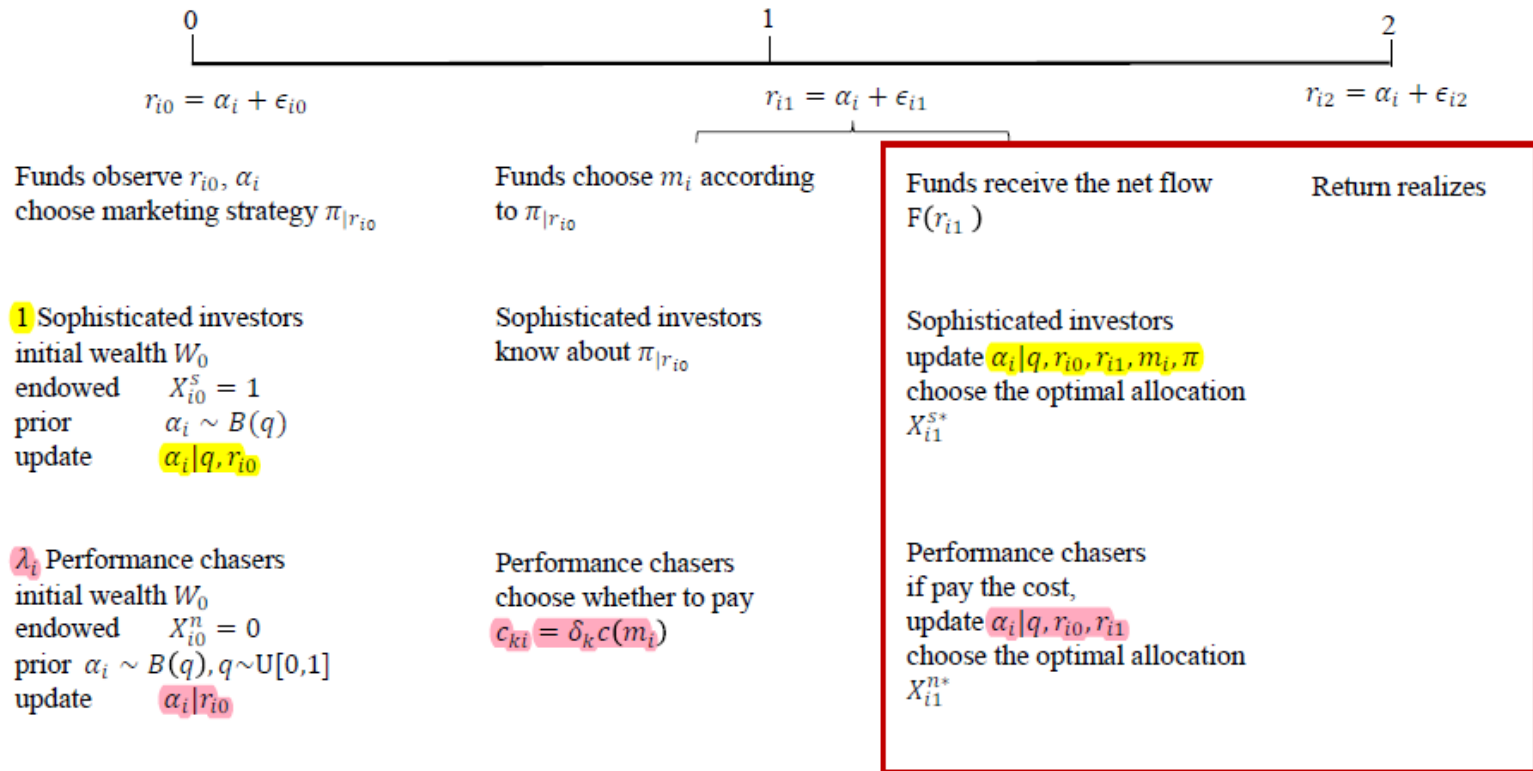
- This paper: only performance chasers who pay the cost invest in funds.
- If not paying the cost, update $\alpha_i | r_{i0}, r_{i1}$ and make portfolio allocation?
- Information acquisition: if marginal benefit of learning $q > \text{cost}$

Model Setup



- If past performance are strong enough, is marketing more/less important?
- Lower marginal benefit of learning q ; more media coverage;
- Take advantage of the good performance and attract investors with high participation cost;

Model Setup



- This paper: only sophisticated investors observe the marketing strategy.
- Why not signaling to all investors? Can performance chasers acquire such information?

Managerial Skill

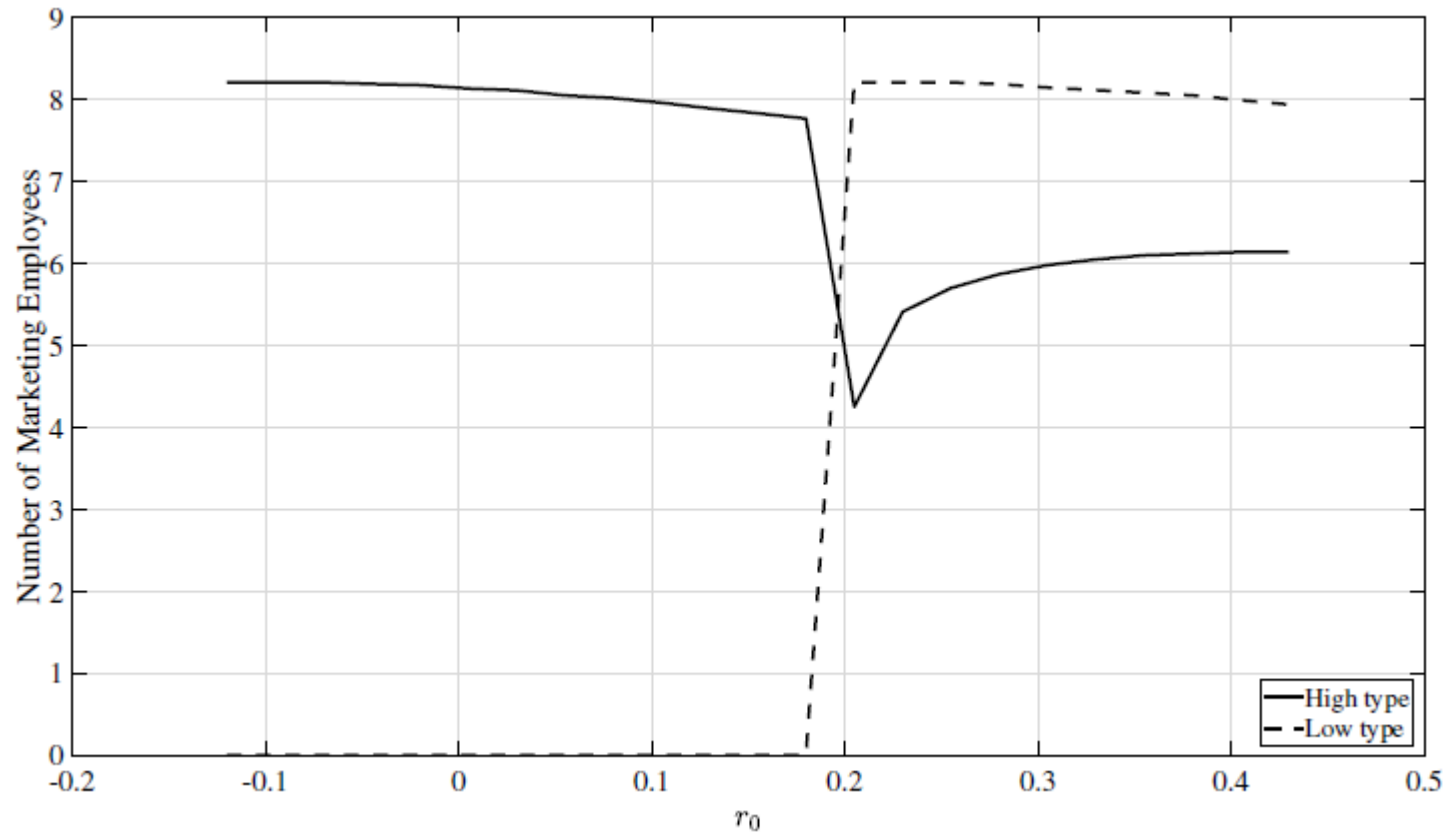
- This paper: mutual fund return $r_{it} = \alpha_i + \epsilon_{it}$, where $\alpha_i \in \{\alpha_l, \alpha_h\}$, $\epsilon_{it} \sim N(0, \sigma_\epsilon^2)$
- Time-invariant skill, persistent performance
- Investors cannot infer the true skill from r_{i0} and r_{i1} .
What if we allow them to observe long-term historical performance?
 - Investors chase Morningstar star ratings (3/5/10-year performance) (Ben-David, Li, Rossi, and Song 2022).
- Reconcile with the lack of persistence in fund performance: time-varying skill; decreasing returns to scale

Managerial Skill

- Empirically, the persistence of marketing strategies can be a better proxy for managerial skill.
- Alternative mechanisms:
- Skilled funds might better allocate the human capital internally: a variety of products, more flexibility; promote non-performance related attributes; launch new funds
- Labor adjustment cost
 - A placebo test to differentiate from signaling: the persistence in other employment share (e.g., investment advisory and research)

Other Testable Predictions: Hiring Decisions

- This paper: low-type funds only hire more marketing employees following good performance.



Other Testable Predictions: Signaling

- This paper: high marketing effort following poor performance signals high-type.

Skill	Low Past Performance	High Past Performance
Low	/	MKT
High	MKT	MKT

	Performance	Assets, Flow, Growth
Vol(MKT)	-	/

- Investors do not directly observe $Vol(MKT)$.
- Does High MKT \times Low Performance predict higher future performance (compared to High MKT \times High Performance)?

Other Testable Predictions: Signaling

- Do sophisticated investors (e.g., institutional share class) respond to such signal by withdrawing less from high-type funds following poor performance?
- Do performance chasers (e.g., retail share class) invest in low-type funds following superior performance?

Extensions

- How does the strategic marketing policy affect the flow volatility and flow-performance sensitivity?
- What if we allow fund fees to increase in marketing effort?
- What if managerial skill is unknown to both the manager and investors (Berk and Green, 2004)?
- Investor type: institutional vs. retail; broker-sold vs. direct-sold

What I Learned...

- Under costly learning and signaling, funds with **persistent** marketing employment strategy perform better.
- Important research question, a rich set of predictions, carefully executed empirical work.