

Discussion of

**Remeasuring Scale in
Active Management**

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Context

- Large literature debating value of active management
 - Many papers test for predictable differences in returns (e.g., Chevalier & Ellison 1999)
 - Others focus on performance persistence... or absence thereof (e.g., Hoberg, Jumar, Prabhala 2018)
- Berk and Green (2004):
 - Skill + Diseconomies of Scale (DoS) → lack of predictable differences in returns & lack of performance persistence
- Existing evidence mixed (partially due to levels vs. logs)
 - Berk & van Binsbergen (2015), Pastor, Stambaugh, Taylor (2015)
 - Reuter & Zitzewitz (RF 2021)

This Paper

- Demonstrates **level-based** measures of DoS, including dollar value added, are biased against active management...
- ... by demonstrating many firms offer institutional vehicle “twins” earning virtually same returns as mutual funds

1995	\$0.57T in MF	\$0.21T in IV twins
2023	\$4.27T in MF	\$3.37T in IV twins

- Filter to identify IV twins → study sample of active equity portfolios where researchers had correct portfolio returns but wrong portfolio AUM “over the entire history”
- **Caveat?** *While level-based measures of DoS approximately half as large, no reduction in log-based measures*

My Assessment?

Paper makes a simple point... convincingly... thanks to lots of data work

My comments focus on limitations and extensions

1. Filter used to hold returns constant necessarily underestimates true level of co-management
2. Can authors say more about selection into IV twins and predictable differences in returns?
3. Should differences in flow-performance between MF and IV have implications for returns?

1. Filter Limitations?

- Assume management team manages both MFs and IVs
- Requiring MF and IV twin have “99% return correlation” will underestimate level of co-managed IV assets if...
 - MF and IV have (slightly) different investment mandates *at any point* during sample
 - MF and IV experience different returns because of uncorrelated flows (e.g., Edelen 1999)
 - MF and IV have same mandate but management team exhibits favoritism towards MF or IV (e.g., Del Guercio, Genc, and Tran 2018)

1. Filter Limitations? (cont.)

- Authors use Morningstar and eVestment to identify twins with same strategy (e.g., Morningstar StrategyID)
 - **Overlap between MS and eV is lower than I expected**
 - 2023Q1: **1954** MF
 - 1012** MF (**51.8%**) have IV twin according MS
 - 1097** MF (**56.1%**) have IV twin according eV
 - 1380** MF (**70.6%**) have IV twin according MS or eV
 - I would like to see more on robustness of main findings for researcher with access to only one data source
- **Alternative:** If we do not want to hold returns constant, we can use US SEC filings to measure non-MF/ETF AUM (at level of manager or management team)

Example of SEC Data of AUM



Mike Feehily
Senior Managing Director
State Street Global Advisors

From SAI for SPDR Russell 1000 ETF

Other Accounts Managed as of June 30, 2016

Portfolio Manager	Registered Investment Company Accounts	Assets Managed (billions) *	Pooled Investment Vehicle Accounts	Assets Managed (billions) *	Other Accounts	Assets Managed (billions) *	Total Assets Managed (billions) *
	Mike Feehily	112	\$ 152.38	382	\$ 484.74	331	\$ 221.35
John Tucker	112	\$ 152.38	382	\$ 484.74	331	\$ 221.35	\$ 858.47
Karl Schneider	112	\$ 152.38	382	\$ 484.74	331	\$ 221.35	\$ 858.47
Mahesh Jayakumar	11	\$ 27.84	104	\$ 60.34	142	\$ 50.23	\$ 138.40
Cynthia Moy	11	\$ 27.84	104	\$ 60.34	142	\$ 50.23	\$ 138.40
James Kramer	11	\$ 27.84	104	\$ 60.34	142	\$ 50.23	\$ 138.40
Joanna Madden	11	\$ 27.84	104	\$ 60.34	142	\$ 50.23	\$ 138.40

* There are no performance fees associated with these portfolios.

MFs & ETFs

Outside MF/ETFs

Can gain insights into extent of side-by-side management of separate accounts (“IV twins”), hedge funds, etc.

1. Filter Limitations? (cont.)

- Del Guercio, Genç, Reuter & Tran (2024) find more missing assets using SEC data...

		Active Equity		Passive	
		2005-2011	2012-2017	2005-2011	2012-2017
AUM/mgr	MF/ETF	2,764	3,144	10,446	20,593
(\$2005 M)	All (SEC)	5,669	5,770	40,459	75,748
	“Missing”	51%	46%	74%	73%

- ... but not a lot more

		Active Equity			
		2005-2011	2012-2017		
AUM	MF	2.75T	3.90T		
(\$T)	MF + IV	4.45T	6.36T		
	“Missing”	38%	39%		

2. Selection into IV Twins?

- **MF with IV twins are different...**
 - MF with IV twins are **3.3** times larger ignoring IV assets and **5.4** times larger including IV assets...
 - ... yet MF with IV twins outperform **32 bp/quarter** after fees
- Reminds me of return difference between direct-sold and broker-sold funds in **Del Guercio & Reuter (2014)** and, more generally, in **Gârleanu & Pedersen (2018)**
- What predicts introduction of IV twin: “[L]arger [MFs] and those that have recently outperformed their benchmarks are more likely to offer [IV twins]” → **true but not entirely satisfying**

2. Selection into IV Twins? (cont.)

- How is decision to offer IV twin related to search costs / market segmentation?
- To what extent do MFs with/without IV twins hold different stocks or pursue different trading strategies (e.g., Evans & Fahlenbrach 2012; van Binsbergen et al. 2024)
 - Evidence on differences in investment horizon is nice start
- Families cross-sub towards MF with IV twins (e.g., Gaspar, Massa, Matos 2006)? Would complicate DoS inferences
- Are MF with IV twins less likely to adopt new strategies in response to poor performance (e.g., Lynch & Musto 2003)

3. Flow-Performance?

- Authors conclude with analysis of flow-performance:
 - “MF flows can only explain a small fraction of variation in IV flows, as reflected by R2 of about 1% to 2% in univariate regressions”
 - “flows into these twin vehicles are largely independent of each other in the cross-section, especially at the fund level”
 - To extent MF and IV experience different flows, will experience different returns (Edelen 1999)... and not be counted as twins
- IV flows are less sensitive to both portfolio performance and style-level flows... but what about risk-adjusted returns?
- Aside: If IV perform monitoring role, does it appear that funds with greater % IV have lower DoS?

Conclusion? Almost a Bullseye

