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Are fund managers' biases hurting investors?

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Questions are being asked about their ability to utilise a data-driven approach while effectively managing their own biases

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The recent volatility in the stock markets, marked by a surge to record highs following favourable exit polls and a subsequent crash on the day of the election results, has raised concerns about the methodologies employed by fund managers. Specifically, questions are being asked about their ability to utilise a data-driven approach while effectively managing their own biases.

Devina Mehra, Founder and CMD of First Global, in a social media post said that for most people, it is virtually impossible to leave aside their incentives (usually gathering AUM or talking up their portfolio) or their political biases and look at data objectively. "Whether blinded by their biases or incentives, these types of reversals only show up that your average fund manager is not fact or data-driven," she wrote.

On Monday, benchmark indices logged their best gains in over three years as investors cheered the exit polls, which predicted a comfortable majority for the BJP-led National Democratic Alliance.

The next day, equity markets crashed after the election results showed that Bharatiya Janata Party would have to rely on its partners to form a government, contrary to exit polls that had predicted a comfortable majority. "Till a day ago, it was that the incumbent government has to come back with a thumping majority for all good things to happen for the economy and Markets. Now the same people are saying that minority and coalition governments are actually pretty good for the stock market and even the macroeconomic outlook," Mehra added.

Too much optimism

Rahul Ghose, CEO of Hedged.in, said the main problem has been far too much optimism in the results which led to some amount of an unrealistic push. Although the outcome of the elections is as expected, the magnitude of the win is what spooked folks on D street. “This is an important lesson for retailers to never be too biased and it is best to be in hedged positions rather than always trying to predict moves. The important point right now at this juncture is that we aren’t out of the woods as yet. Unless Nifty does a firm close above 23,000, we still have exposure on the downside which will get accelerated below 21,800.”

Siddharth Oberoi, Fund Manager at Prudent Equity ACE Fund, offered a different perspective, he said, “There has been intense speculation in the Indian markets over the last three years. As these general elections were quite significant due to expectations of policy continuity, large bets were placed in the F&O segment. It is this segment that is most influenced. Seasoned fund managers mostly look at individual companies and then a portfolio is built around them. These companies are studied by them, and their business models are well understood. Hence, I do not think that most fund managers reacted either way based on the exit polls or the results. Maybe a small portion of capital was deployed or withdrawn based on the changing circumstances.”

Manish Chowdhury, Head of Research at StoxBox, expressed, “Our sense is that most of the fund managers and brokers were convinced about the corporate earnings trajectory and believed that the volatility was more short-term in nature which would recede going forward. The sharp drawdowns in many frontline stocks (both cash and F&O) yesterday appeared to be algorithm-driven and were triggered on falling below crucial levels. We believe that markets would return to sanity as the structural theme and fundamental thesis of Indian equities remain intact. We anticipate more clarity on the policy front to emerge following the government formation and the Budget release which is expected in the first half of July.”