

# The Rise of Passive Investing

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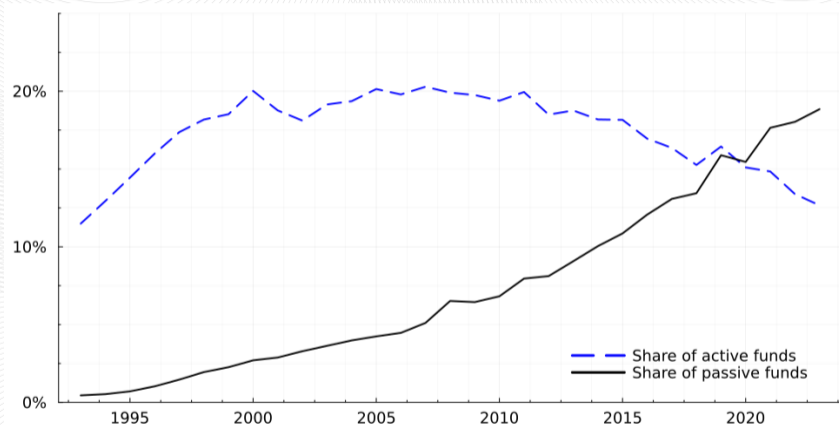
# Passive Investing in the Data

The Role of Competition for Passive Investing

Passive Investing & Volatility, Price Efficiency, Liquidity

Discussion

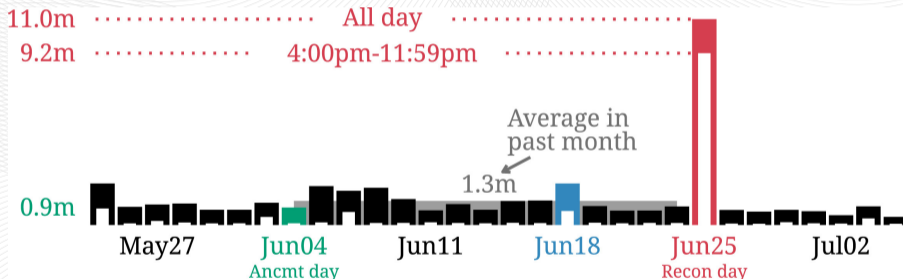
# U.S. Mutual Funds and ETFs



- Data source: ICI Factbook 2024

# Excess Recon Day Volume

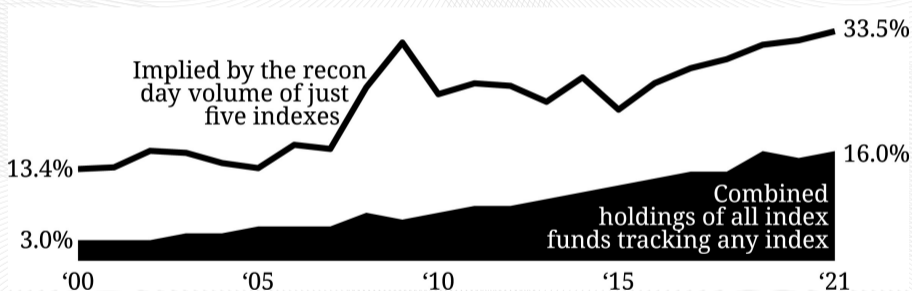
- YETI moved from Russell 2000 to Russell 1000 on June 25, 2021
- large spike of trading volume on reconstitution date (passive funds trade)



- Data source: Chincó and Sammon (2024, Journal of Financial Economics)

# Excess Recon Day Volume

- excess recon day volume + weights in index  $\Rightarrow$  infer how much indexing
- 5 indices: S&P 500, S&P MidCap 400, Russell 1000, Russell 2000, Nasdaq 100



- Data source: Chincó and Sammon (2024, Journal of Financial Economics)

**How does the portfolio of a financial institution line up with market caps?**

→ “A lot” ⇔ passive institution



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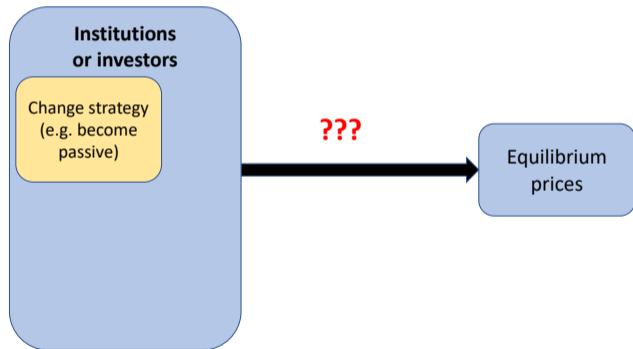
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# Investor Competition Matters!

Effect of a change in strategy of **some** institution on **equilibrium** asset prices?

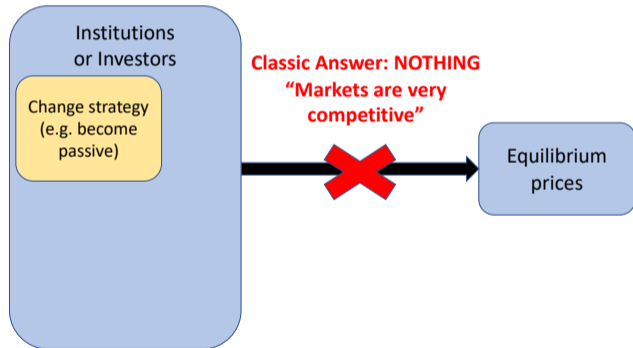
- The rise of passive investing





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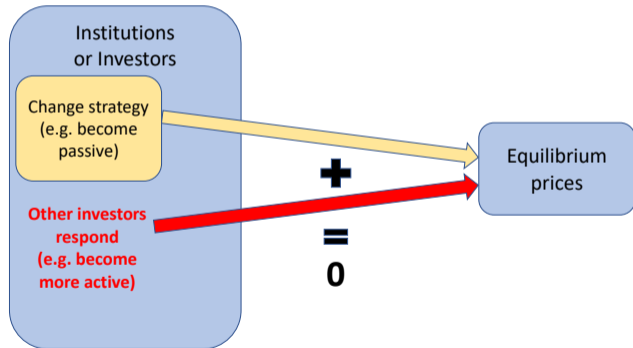
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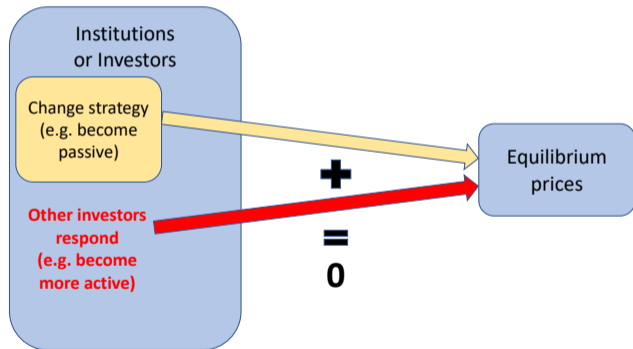
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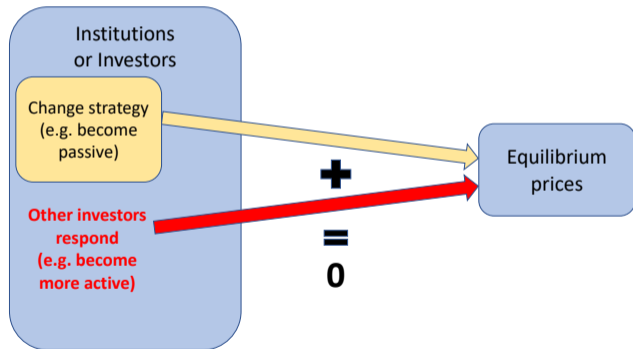


→ How large is the strategic response?

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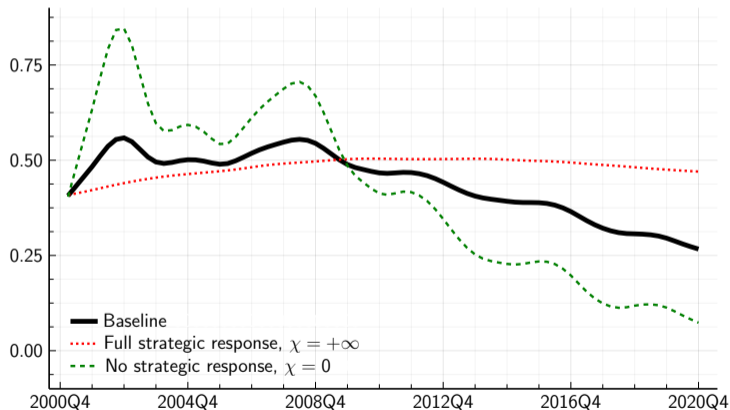


→ How large is the strategic response?

→ 2/3 of direct effect

What would have been the effect of passive investing based on competition?

- y-axis: our measure of how “efficient” markets are



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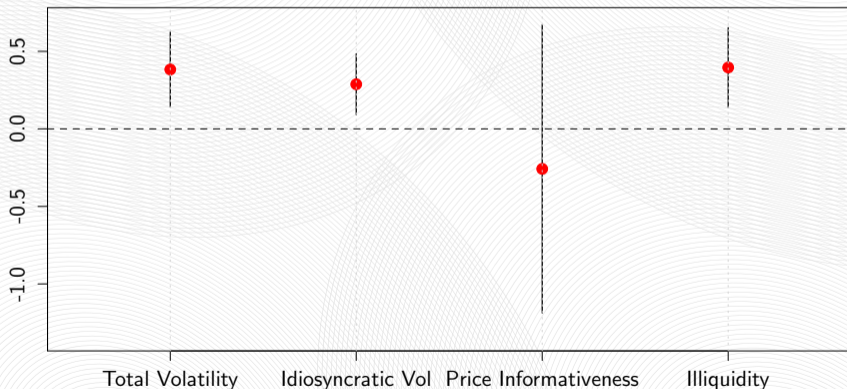
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The rise of passive investing decreased our efficiency measure by 11%

our measure  $\downarrow \Rightarrow$  volatility  $\uparrow$ , price informativeness  $\downarrow$ , illiquidity  $\uparrow$



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