



M O M E N T U M

Follow the Leader: Peer Effects in Mutual Fund Portfolio Decisions

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Working paper

This paper provides evidence of cross-autocorrelations in trades of mutual funds. It shows that funds “follow the leaders:” trades of well-performing funds are statistically and economically important determinants of subsequent portfolio decisions of the remaining managers. The evidence suggests that poorly performing funds engage in mimicking more than funds with better performance.

The author suggests that follower funds believe that leaders have better skill or information. Potentially, leaders are not able to fully impound their new information into stock prices: they may not be large enough, or decide against a large investment for reasons of diversification. Leaders’ private information is revealed when they disclose their portfolio composition. The results also suggest a possible link between “follow the leader” behavior and short-term momentum in stock returns.

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