

POLITICAL INVESTING: THE COMMON STOCK INVESTMENTS OF MEMBERS OF CONGRESS 2004-2007

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I. INTRODUCTION

Talk a bit about the rules and the concerns. The current pending bill is:

GovTrack.us. H.R. 2341–110th Congress (2007): Stop Trading on Congressional Knowledge Act, GovTrack.us (database of federal legislation) ;<http://www.govtrack.us/congress/bill.xpd?bill=h110-2341>; (accessed Nov 30, 2008)

The rules are described in Public (Self)-Service: Illegal Trading on Confidential Congressional Information Andrew George. in the bib files as: george2008.

II. TRADING ON POLITICAL INFORMATION

There exists surprisingly little research about the financial transactions of politicians and US Congressmen in particular. Boller (1995) examined the FDRs of 111 randomly selected Congressmen who traded common stocks in the 1991-1993 period. He found that 83 Members held investments in companies that were potentially directly affected by ongoing legislation.

Ziobrowski et al. (2004) conducted the most comprehensive study to date. They investigated the common stock investments of US Senators drawing upon a dataset of 6,052 sell and buy transactions for the years 1993 to 1998. In their data, trades were highly concentrated; about 30 Senators traded in each year and overall four Senators accounted for almost half of all transactions.¹ Ziobrowski et al. asked whether trading Senators outperform the market, focusing on long run abnormal returns. As a first step, they conducted graphical event study analysis comparing daily cumulative abnormal returns (CAR) in a 255 day window before and after the transaction dates. An approximate reproduction of their finding is presented in figure 1, which shows the CARs summed over all transactions. The figures indicates an extremely fortunate timing of the Senators' trades. Stocks that they sold experienced a 25 percent run-up in the CARs during the 12 month prior to the

¹Ziobrowski et al. matched transactions from the FDRs with returns data from the Center for Research and Security Prices (CRSP) database for common stocks traded in NYSE, AMEX, and NASDAQ. They noted that “the care used to fill out the reports varies widely. Some are typed, some are handwritten, some include monthly financial statements from their brokerage firms, and some use abbreviations and terms that are impossible to decipher. Thus extraction of the data was very difficult and despite our best efforts may have resulted in occasional errors.” (Ziobrowski et al. 2004, pg. 3).

sell date and remained fairly flat thereafter. Stocks that they purchases showed the opposite pattern; CARs increased by only 3 percent prior to the buying date, but by almost 28 percent in the year following the transaction.

As a second step, Ziobrowski et al. also ran formal tests based on a monthly calender-time portfolio approach with the Fama-French three factor model and the Capital Asset Pricing Model (CAPM). Averaging over all transactions, they considered six portfolios: a trade-volume weighted and equally weighted portfolio of the buy transactions, a trade-volume weighted and equally weighted portfolio of the sell transactions, and a trade-volume weighted and equally weighted hedged portfolio in which the buy transactions were held long and the sell transactions were held short. They found positive abnormal returns for the buy portfolios and the hedged portfolios. The results for the hedged portfolios were also generally significant at conventional levels (except the Fama-French Alpha from the equal weighted portfolio). Stock purchased by Senators on average outperformed the market by about 85 basis points per month or even 97 basis points in the hedged portfolio. For the buy portfolios the results were significant for the Fama-French Alphas, but not the Jensen's Alphas from the CAPM. They also found negative abnormal returns for the sell portfolios. Stocks sold by Senators on average under-performed the market by 12 basis points, but the magnitudes were generally smaller and the results were not significant at conventional levels. In general, the alphas were much higher for the trade-weighted than the equal weighted portfolios indicating that Senators invested more heavily in the most profitable transactions. They also conducted some subgroup analysis and found no reliable differences between the returns for the investments of Democratic and Republican Senators. Moreover, stocks purchased by Senators with least seniority (in office less than 7 years) showed higher returns than those bought by Senators with the highest seniority (in office more than 16 years). They also reported that in separate tests abnormal returns vary widely across years, in particular they found no abnormal returns for the years 1997 and 1998 when trading activity dropped in their sample (presumably due to the retirement of a few very actively trading senators).

Overall, Ziobrowski et al. concluded that their results show that Senators use a substantial informational advantage in their trading. The sheer magnitude of their findings seem stunning. As a rough comparison Barber & Odean (2000) who measured the common stock returns for a large sample of randomly selected household over the 1991 to 1996 period found that they under-performed the market by 12 basis points.

III. DATA

We obtained data from 2,235 annual FDRs of all 650 Congressmen that served between 2004 and 2007 from the Center of Responsive Politics (CRP).² The FDRs contain 130,215 reported assets holdings with an approximate value of \$9.2 billion and 68,346 asset transactions with an approximate value of about \$3 billion. This includes the reported assets of a Member's spouse and or dependent children. Members have to disclose the value of the assets holdings and transactions within broad ranges: \$1,001-\$15,000; \$15,001-\$50,000; \$50,001-\$100,000; \$100,001-\$250,000; \$250,001-\$500,000; \$500,001-\$1,000,000; and over \$1,000,000. For all value based analysis we rely on midpoints and cap all transactions above \$1 million.³

Since our analysis focuses on common stock investments, we eliminated all assets and transactions that were not securities (mostly real estate transactions and investments in bonds) and corrected a few incorrect transaction dates. For the remaining assets and transactions we matched the name to a ticker symbol and retrieved daily quotes from the Center for Research and Security Prices (CRSP) database. CRSP only covers companies that were publicly traded on NYSE, AMEX, or NASDAQ, so this led to the exclusion of other exchanges and mutual funds.⁴ Overall we ended up with 54,003 stock holdings with

²The average number of FDRs per Member is about 3.5 since not all Members serve for the entire four years: 70 % have 4 reports, 12 % have 3 reports, 9 % have 2 reports, and 9 % have only 1 report. There is also a very small number of missing reports.

³This follows Ziobrowski et al. except that they capped at \$250,000.

⁴A very small number of companies listed on those exchanges did not return quotes. Notice that we do not consider privately held companies despite that the fact that there are several examples of links between private companies and legislators. Numerous such cases are listed in the Citizens for Responsibility and Ethics in Washington's annual reports (2005-2008) on the "Most Corrupt Members of Congress." See <http://www.crewsmostcorrupt.org/report>.

an approximate value of \$2.5 billion and 45,135 stock trades (20,025 buys and 25,110 sells) worth about \$1 billion in total. The stocks cover a total of 3,132 unique companies, about 58 % are listed on the NYSE, 38 % on the NASDAQ, and 3 % on the AMEX. About 88 % of the companies are U.S. companies.

Figure 2 shows the empirical cumulative distribution functions (CDF) of the matched stock holdings and stock transactions (buys plus sells) of each Member summed over the 2004-2007 period. The upper panel shows the CDFs for the overall number of a Member's holdings and transactions, the lower panel shows the CDFs for overall value of a Member's holdings and transactions. The functions show that both holdings and transactions are fairly concentrated. 27 % (50 %) of the Members report zero stock holdings (transactions) over our 4 year period. The median number of stocks held (traded) per Member was 7 (1). About 15 % (10 %) of the Members hold (trade) more than 100 stocks and the 20 most active Members, each with more than 500 holdings and transactions each account for about 31 % of all holdings and 37 % of all reported transactions in our period. The distribution of the value of the stock holdings and transactions is highly skewed. Of the holdings (transactions) about 50 % (77 %) are in the range between \$1,001-\$15,000; 12% (12 %) are within \$15,0001-\$50,000; 4 % (4 %) are within \$50,001-\$100,000; and 7 % (3 %) are larger than \$100,001. The average value of the stock holdings (transaction volume) per Member is about \$3.8 millions (\$1.6 million). The median Member held stocks worth of \$113,000 and traded with a volume of \$4000. About 25 % of the Members hold more than \$1 million worth of stock and about 14 % trade more than one million over our four year period. The top 20 Members that each report more than 20 million of holdings and more than 9 million of trading volume account for about 60 % (57 %) of the total value of all holdings (transactions).

IV. CONCLUSION

$$R_{p,t} - R_{f,t} = \alpha_i + \beta(R_{m,t} - R_{f,t})$$

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- Boller, G. (1995), Taking stock in congress. Published in *Mother Jones*, Sept Issue.
- Ziobrowski, A., Cheng, P., Boyd, J. & Ziobrowski, B. (2004), 'Abnormal Returns from the Common Stock Investments of the US Senate', *Journal of Financial and Quantitative Analysis* **39**(4), 661–676.

TABLES

Figure 1: Figure 1 from Ziobrowski et al. (2004): Daily Cumulative Abnormal Returns for Common Stocks Bought and Sold by US Senators 1993-1998 (approximate reproduction).

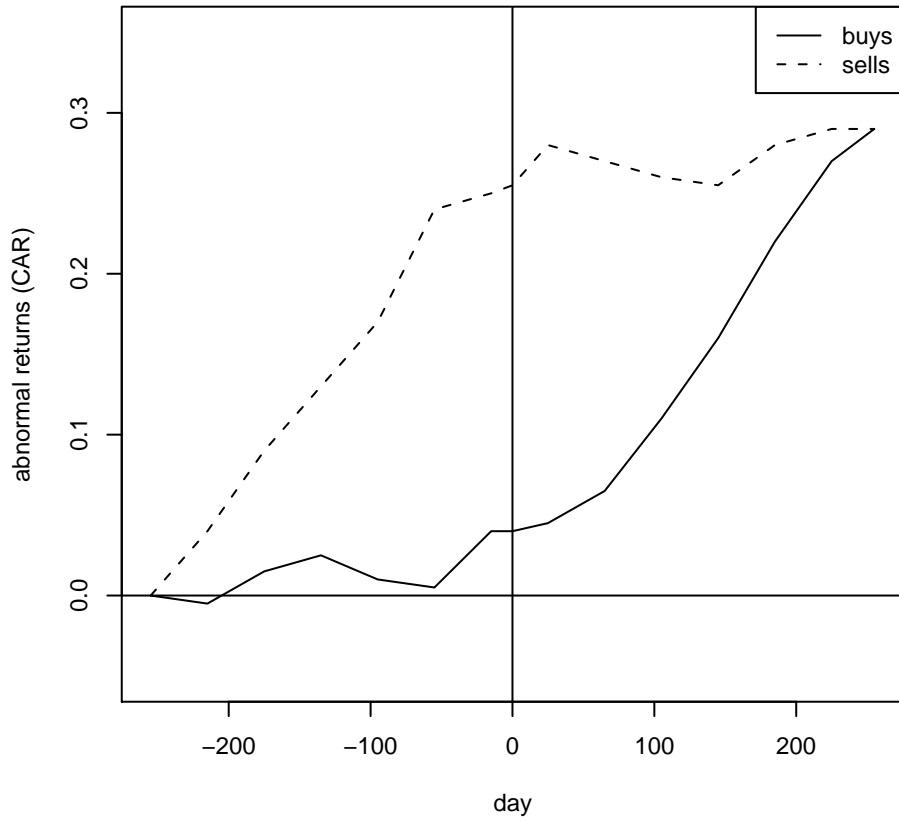


Table 1: Top 50 Members by Number of Stock Holdings

name	Stock Holdings		Stock Trades		rank
	number	value (\$K)	number	value (\$K)	
Carolyn McCarthy (D-NY)	4199	3267	3237	3735	1
Jane Harman (D-Calif)	3286	126578	2174	81599	2
Hal Rogers (R-Ky)	2485	5815	1914	2923	3
Kenny Ewell Marchant (R-Texas)	1934	15541	3819	25652	4
Elizabeth Dole (R-NC)	1665	590100	1140	14592	5
Dianne Feinstein (D-Calif)	1355	98636	2	1750	6
Tom Osborne (R-Neb)	1217	9538	1442	11536	7
Lamar Smith (R-Texas)	1215	3233	1090	2454	8
Amo Houghton (R-NY)	1058	7233	0	0	9
Mark Dayton (D-Minn)	1052	20873	738	6974	10
F. James Sensenbrenner Jr. (R-Wis)	1046	50524	328	8873	11
John Kerry (D)	935	368343	2456	311337	12
Michael McCaul (R-Texas)	823	27128	894	14393	13
Jon L. Kyl (R-Ariz)	816	994	481	498	14
Nick Rahall (D-WVa)	801	4786	1574	2709	15
Robin Hayes (R-NC)	793	217650	30	505	16
Jeff Bingaman (D-NM)	785	6636	2110	27487	17
Shelley Berkley (D-Nev)	727	5960	342	3297	18
Nancy L. Johnson (R-Conn)	611	3552	227	1890	19
Jim Moran (D-Va)	591	6924	1915	18200	20
Rodney Frelinghuysen (R-NJ)	575	68673	205	11499	21
Jim Kolbe (R-Ariz)	571	3840	364	2560	22
Jim Leach (R-Iowa)	544	10389	772	10947	23
John W. Warner (R-Va)	496	7746	390	4549	24
Mary Bono (R-Calif)	495	5109	922	7523	25
Tom Coburn (R-Okla)	469	3048	322	2957	26
Joe Knollenberg (R-Mich)	453	3665	33	496	27
John Campbell (R-Calif)	449	3411	198	5243	28
Judy Biggert (R-Ill)	410	11792	196	3431	29
Vernon Buchanan (R-Fla)	401	8662	635	16259	30
Donald J. Cazayoux (D-La)	385	172	182	288	31
Zoe Lofgren (D-Calif)	383	2415	575	4781	32
Michael N. Castle (R-Del)	359	4827	101	923	33
Jack Kingston (R-Ga)	349	1727	159	1734	34
Bob Corker (R-Tenn)	348	6942	0	0	35
Pat Roberts (R-Kan)	336	2068	201	1943	36
Randy Neugebauer (R-Texas)	315	1485	614	4937	37
James Webb (D-Va)	313	1826	0	0	38
Eric Cantor (R-Va)	296	5453	114	1549	39
Chris Chocola (R-Ind)	293	26639	1320	77289	40
Trent Lott (R-Miss)	280	843	8	49	41
Frank R. Lautenberg (D-NJ)	271	11486	126	10149	43
Paul Ryan (R-Wis)	271	3430	103	947	43
Fred Upton (R-Mich)	270	26149	10	105	44
Thad Cochran (R-Miss)	262	2281	487	4480	45
Michael R. Turner (R-Ohio)	255	1865	68	536	46
David Vitter (R-La)	249	3842	69	668	47
James L. Oberstar (D-Minn)	240	15618	249	25409	48
Lloyd Doggett (D-Texas)	238	12360	22	358	49
Dave Camp (R-Mich)	233	8215	115	2634	50

Figure 2: Cumulative Distribution Functions: Stock Holdings and Stock Transactions of Members 2004-2007

