Introduction

- Political polarization and partisanship are on the rise
  - “Partisan perceptual screen” (Campbell et al. (1960))
  - Partisan perception in the formation of economic expectations (e.g., Gerber and Huber (2009) and Mian et al. (2017))

Question: Does partisan perception affect economic decisions?

Evidence from households mixed
- Spending behavior: yes (Makridis (2018)) and no (McGrath (2017), Mian et al. (2017))
- Portfolio choice: yes (Meeuwis et al. (2018))
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- So far, **no evidence on economic decisions in high-stake environments**
○ **This paper:** Does political alignment with the president affect decisions by finance professionals?

○ **Setting:** credit rating analysts

1. We can link credit rating decisions to individual analysts (Fracassi et al. (2016))

2. Credit ratings matter for firms’ cost of capital, financing and investment policies (e.g., Kisgen (2006, 2009), Almeida et al. (2017))

3. Requires *long-term* forecasts of credit risk

4. Multiple analysts rate the *same firm* at the *same point in time*
Introduction

What do we find?

This paper
Introduction

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1. Analysts who are not affiliated with the president’s party downward-adjust ratings more by 11.4%
Introduction This paper

- What do we find?

1. Analysts who are not affiliated with the president’s party downward-adjust ratings more by 11.4%

   - Divergence in rating decisions by Democratic and Republican analysts around the Trump election
Introduction

What do we find?

1. Analysts who are not affiliated with the president’s party downward-adjust ratings more by **11.4%**

- Divergence in rating decisions by Democratic and Republican analysts around the **Trump election**
- Firms rated by misaligned analysts **lose 0.52%–0.62% more** of their market capitalization over a single presidential term
- Firms **experience and increase of 5.9 bps more** in bond yields over one presidential term
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2. Mechanism: differences in beliefs about aggregate economic conditions
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2. Mechanism: differences in beliefs about aggregate economic conditions
   - Conducted online survey of credit rating analysts
   - Effect is larger when views of economic conditions are more politically polarized, and for cyclical firms
Part I: **Rating actions on all U.S. corporate debt issuers** between 2000Q1–2018Q1
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- Rating actions:
  - Moody’s: Moody’s DRD
  - Standard & Poor’s: S&P RatingXpress
  - Fitch: Mergent FISD
Data Rating actions

○ Part I: Rating actions on all U.S. corporate debt issuers between 2000Q1–2018Q1

○ Rating actions:
  – Moody’s: Moody’s DRD
  – Standard & Poor’s: S&P RatingXpress
  – Fitch: Mergent FISD

○ Match to a press release that contains the name(s) of the analyst(s) covering the firm
  – Usually contain two names, the lead analyst and the rating committee chair or secondary analyst
○ Part II: **Data on party affiliation**
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○ Source: Voter registration records from New York City, New Jersey, and Illinois
Part II: **Data on party affiliation**

- Source: Voter registration records from New York City, New Jersey, and Illinois
- Contain full name, age / date of birth, address, party affiliation, election date, election type
- The elections covered are general, primary, and municipal elections
- **Part II: Data on party affiliation**

- **Source:** Voter registration records from New York City, New Jersey, and Illinois

- **Contain full name, age / date of birth, address, party affiliation, election date, election type**

- **The elections covered are general, primary, and municipal elections**

- **Final sample:** 557 analysts covering 1,984 firms (match rate of 46%)
Partisan Professionals

Kempf and Tsoutsoura
Data Descriptives

Kempf and Tsoutsoura
Partisan Professionals

8 / 23
<table>
<thead>
<tr>
<th></th>
<th>N</th>
<th>Mean</th>
<th>Std. Dev.</th>
<th>0.25</th>
<th>Median</th>
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<td></td>
<td></td>
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<td></td>
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<td>0.000</td>
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<td><strong>Partisan Bias</strong></td>
<td></td>
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<tr>
<td>Ideological mismatch</td>
<td>76,969</td>
<td>0.370</td>
<td>0.483</td>
<td>0.000</td>
<td>0.000</td>
<td>1.000</td>
</tr>
</tbody>
</table>

- Rating change = difference (in notches) between rating at the end of the calendar quarter and rating at the beginning of the quarter
  - Ratings transformed into cardinal scale, starting with 1 for Aaa and ending with 21 for C
  - I.e., positive change = downgrade
- Ideological mismatch = 1 if party affiliation does not match the president’s, 0 otherwise
Empirical Strategy

- Has to address the following issues:

   - Non-random matching of analysts to firms
   - Agency differences in rating methodologies
   - Time-invariant characteristics of analysts with different affiliations

\[ \Delta R_{it} = \alpha_{ft} + \alpha_{p} + \beta \text{Ideological mismatch}_{it} + \gamma'X_{it} + \epsilon_{it} \]

- Additional fixed effects (e.g., agency × quarter f.e.)

- Why changes instead of levels?
  - Analysts may respond gradually rather than instantly to a change in the president
Empirical Strategy

- Has to address the following issues:
  1. Non-random matching of analysts to firms
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- \( \alpha_{ft} \): firm \times quarter f.e.
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- Why changes instead of levels?
  - Analysts may respond gradually rather than instantly to a change in the president
Results

Univariate

Adjusted rating change

BushW 1  BushW 2  Obama 1  Obama 2  Trump 1

Republican Analyst  Democrat Analyst  Unaffiliated Analysts

Kempf and Tsoutsoura
Partisan Professionals
### Rating Change

<table>
<thead>
<tr>
<th></th>
<th>(1)</th>
<th>(2)</th>
<th>(3)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ideological mismatch</td>
<td>0.0168</td>
<td>0.0170</td>
<td>0.0134</td>
</tr>
<tr>
<td></td>
<td>(4.18)</td>
<td>(4.26)</td>
<td>(3.79)</td>
</tr>
<tr>
<td>Tenure</td>
<td>0.0001</td>
<td>-0.0006</td>
<td>-0.0004</td>
</tr>
<tr>
<td></td>
<td>(0.03)</td>
<td>(-0.23)</td>
<td>(-0.15)</td>
</tr>
<tr>
<td>No. of firms covered</td>
<td>-0.0001</td>
<td>0.0001</td>
<td>-0.0000</td>
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<tr>
<td></td>
<td>(-0.10)</td>
<td>(0.05)</td>
<td>(-0.02)</td>
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<tr>
<td>Observations</td>
<td>49,792</td>
<td>49,792</td>
<td>49,790</td>
</tr>
<tr>
<td>$R^2$</td>
<td>0.804</td>
<td>0.804</td>
<td>0.808</td>
</tr>
<tr>
<td>Firm × Quarter FE</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Agency FE</td>
<td>Yes</td>
<td>No</td>
<td>No</td>
</tr>
<tr>
<td>Agency × Sector FE</td>
<td>No</td>
<td>Yes</td>
<td>No</td>
</tr>
<tr>
<td>Agency × Quarter FE</td>
<td>No</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>Party Affiliation FE</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td></td>
<td>(1)</td>
<td>(2)</td>
<td>(3)</td>
</tr>
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</tr>
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<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Agency FE</td>
<td>Yes</td>
<td>No</td>
<td>No</td>
</tr>
<tr>
<td>Agency $\times$ Sector FE</td>
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<td>No</td>
</tr>
<tr>
<td>Agency $\times$ Quarter FE</td>
<td>No</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>Party Affiliation FE</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
</tbody>
</table>

- Analysts who do not support the president’s party on average downward-adjust more by **0.013 notches per quarter** (0.21 notches over four years)
## Results

<table>
<thead>
<tr>
<th></th>
<th>Coeff</th>
<th>t-statistic</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Baseline</strong></td>
<td>0.0134</td>
<td>3.79</td>
</tr>
</tbody>
</table>

### Panel A: Alternative dependent variables

<table>
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<tr>
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<tr>
<td>Rating change indicator</td>
<td>0.0110</td>
<td>3.88</td>
</tr>
<tr>
<td>Downgrade</td>
<td>0.0064</td>
<td>3.24</td>
</tr>
<tr>
<td>Upgrade</td>
<td>-0.0046</td>
<td>-2.21</td>
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</table>

### Panel B: Alternative definitions of ideological mismatch

<table>
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<tr>
<th></th>
<th>Coeff</th>
<th>t-statistic</th>
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</thead>
<tbody>
<tr>
<td>Use only party affiliation from presidential elections</td>
<td>0.0144</td>
<td>2.75</td>
</tr>
<tr>
<td>Add party affiliation from political contributions</td>
<td>0.0135</td>
<td>4.36</td>
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</table>

### Panel C: Estimation

<table>
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<tr>
<th></th>
<th>Coeff</th>
<th>t-statistic</th>
</tr>
</thead>
<tbody>
<tr>
<td>Triple-cluster standard errors (analyst, firm and quarter)</td>
<td>0.0134</td>
<td>4.33</td>
</tr>
<tr>
<td>Firm-agency level</td>
<td>0.0298</td>
<td>3.82</td>
</tr>
<tr>
<td>Weighted least squares</td>
<td>0.0125</td>
<td>3.35</td>
</tr>
<tr>
<td>Add Analyst FE</td>
<td>0.0108</td>
<td>2.40</td>
</tr>
<tr>
<td>Agency × Sector × Quarter FE</td>
<td>0.0087</td>
<td>2.82</td>
</tr>
<tr>
<td>Add NBER Recession × Party affiliation FE</td>
<td>0.0150</td>
<td>4.03</td>
</tr>
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</table>
Presidential Elections

- We conduct an event study around presidential elections

- We focus on presidential elections where the party of the president changes (i.e., the 2000, 2008, and 2016 election)
We conduct an event study around presidential elections

We focus on presidential elections where the party of the president changes (i.e., the 2000, 2008, and 2016 election)
Presidential Elections

[Graph showing data trends over event quarters, with emphasis on quarter 0 to +4]

Kempf and Tsoutsoura

Partisan Professionals
We conduct an event study around the 2016 presidential election.
We conduct an event study around the 2016 presidential election

Unique setting:
We conduct an event study around the 2016 presidential election.

Unique setting:

- Unexpected outcome
- Candidates had very different views on economic policy (Meeuwis et al. (2018))
- Election date did not overlap with other major economic events
2016 Presidential Election

- Does the rating behavior of Democratic and Republican analysts change around the election?
Does the rating behavior of Democratic and Republican analysts change around the election?
Price and Real Effects

- Potential consequences of analysts’ partisan perception:
  - **Stock prices**
    - Estimate abnormal stock returns around rating-change announcements
    - Result: replacing an aligned analyst with a misaligned analyst leads to a negative abnormal stock return of 0.52–0.62% over 4 years
  - **Bond Yields**
    - Estimate change in yields around rating-change announcements
    - Result: replacing an aligned analyst with a misaligned analyst leads to a 5.9% basis points increase over 4 years
  - **Analyst accuracy**
    - Misaligned analysts less accurate
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3. Analyst accuracy
   - Misaligned analysts less accurate
<table>
<thead>
<tr>
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<tbody>
<tr>
<td></td>
<td>4Q</td>
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<tr>
<td></td>
<td>(1)</td>
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<tr>
<td>Ideological mismatch</td>
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<tr>
<td></td>
<td>(-1.15)</td>
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<tr>
<td>Mismatch $\times$ Rating change</td>
<td>-0.2724</td>
</tr>
<tr>
<td></td>
<td>(-2.04)</td>
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<tr>
<td>Rating change</td>
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</tr>
<tr>
<td></td>
<td>(0.09)</td>
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<tr>
<td>Observations</td>
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</tr>
<tr>
<td>$R^2$</td>
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</tr>
<tr>
<td>Agency $\times$ Quarter FE</td>
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<tr>
<td>Median lagged rating $\times$ Quarter FE</td>
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</tr>
<tr>
<td>Party affiliation FE</td>
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<tr>
<td>Firm controls</td>
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## Price and Real Effects

### Accuracy

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<th>12Q (3)</th>
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<td>(-0.30)</td>
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<td>Mismatch × Rating change</td>
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<tr>
<td></td>
<td>(-2.04)</td>
<td>(-2.48)</td>
<td>(-1.58)</td>
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<td>(-1.29)</td>
<td>(-1.19)</td>
</tr>
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<td>13,573</td>
<td>11,706</td>
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<tr>
<td>R²</td>
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<td>0.659</td>
<td>0.648</td>
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<tr>
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<td>Yes</td>
<td>Yes</td>
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<td>Yes</td>
<td>Yes</td>
</tr>
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<td>Yes</td>
<td>Yes</td>
</tr>
</tbody>
</table>

- Consistent with an alternative measures of accuracy
Main results show that analysts’ political alignment with the president affects credit ratings.

Potential mechanism: differences in beliefs about aggregate economic conditions

- See existing survey evidence from households (e.g., Gerber and Huber (2009))
- Additional suggestive evidence:
  1. Online survey of credit rating analysts
  2. Effect driven by firms and industries with high market betas
  3. Effect is stronger when political polarization in views of economic conditions is high
Mechanism

- Main results show that analysts’ political alignment with the president affects credit ratings.
- Potential mechanism: differences in beliefs about aggregate economic conditions.
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Additional suggestive evidence:

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3. Effect is stronger when political polarization in views of economic conditions is high.
Conducted survey of 91 current and former credit rating analysts (57 valid responses)

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  — “How would you rate economic conditions in this country today — as excellent, good, only fair, or poor?”
  — The responses to the question are converted into a numerical scale that ranges from 1 (poor) to 4 (excellent)
Conclusion

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  - Causal effect of party affiliation versus proxy for ideological differences
- Suggests partisan perception may have real effects