How the Largest Funds Fared

Data provided by LIPPER

Performance numbers are total returns (changes in net asset values with reinvested distributions) as of April 28; assets are as of March 31. All data are final.

The Largest Stock Mutual Funds

			Total Return (%)				
					Annualized		
Fund	Ticker	Assets ($ billions)	April	1-year	3-year	5-year	10-year
Vanguard TSM Idx;Adm	VTSAX	549.59	1.1	18.6	10.1	13.5	7.4
Vanguard 500 Index;Adm	VFIAX	310.71	1.0	17.9	10.4	13.6	7.2
Vanguard Tot I Stk;Inv	VGTSX	262.53	2.2	13.6	1.3	5.6	1.2
SPDR S&P 500 ETF	SPY	241.04	1.0	17.8	10.4	13.5	7.1
Vanguard Instl Indx;Inst	VINIX	222.54	1.0	17.9	10.5	13.7	7.2
American Funds Gro;A	AGTHX	156.22	2.0	20.7	11.3	14.2	7.4
American Funds EuPc;R-6	RERGX	132.38	3.2	15.1	3.3	7.4	N.A.
Fidelity 500 Idx;Pr	FUSVX	118.07	1.0	17.9	10.4	13.6	7.1
Fidelity Contrafund	FCNTX	108.47	2.8	18.6	11.4	13.1	8.7
American Funds Bal;A	ABALX	107.79	1.0	11.0	7.5	10.1	6.7
American Funds Inc;A	AMECX	104.99	0.2	10.6	5.5	9.0	5.3
American Funds CIB;A	CAIBX	103.07	0.8	7.6	3.9	7.2	4.0
iShares:Core S&P 500	IVV	101.82	1.0	17.9	10.4	13.6	7.1
Vanguard Wellington;Adm	VWENX	98.35	0.8	12.0	7.2	9.9	6.9
American Funds Wash;A	AWSHX	89.59	0.9	15.9	8.8	12.7	6.5
American Funds CWGI;A	CWGIX	86.51	1.9	14.6	4.9	9.8	4.6
American Funds FInv;A	ANCFX	84.93	1.2	18.9	10.8	13.6	7.2
American Funds ICA;A	AIVSX	84.41	0.8	15.8	9.3	13.2	6.5
Vanguard Md-Cp Idx;Adm	VIMAX	83.60	1.2	17.5	9.4	13.3	7.6
Franklin Cust:Inc;A	FKINX	82.94	...	14.2	2.8	7.3	4.9

The Largest Bond Mutual Funds

			Total Return (%)				
					Annualized		
Fund	Ticker	Assets ($ Billions)	April	1-year	3-year	5-year	10-year
Vanguard Tot Bd;Adm	VBTLX	177.90	0.8	0.8	2.6	2.2	4.3
Vanguard Tot Bd II;Inv	VTBIX	123.92	0.8	0.6	2.5	2.1	N.A.
PIMCO:Income;Inst	PIMIX	79.08	0.7	9.4	6.0	8.2	9.1
Met West:Total Return;I	MWTIX	78.56	0.8	1.2	2.6	3.6	5.8
Vanguard Tot Itl Bl;Adm	VTABX	77.26	0.6	1.9	4.0	N.A.	N.A.
PIMCO:Tot Rtn;Inst	PTTRX	73.58	0.9	2.8	2.8	2.8	5.7
Vanguard Sh-Tm Inv;Adm	VFSUX	59.56	0.4	1.8	2.0	2.1	3.3
DoubleLine:Tot Rtn;I	DBLTX	54.22	0.8	2.0	3.3	3.6	N.A.
Vanguard Int-Tm TxEx;Adm	VWIUX	51.58	0.7	0.1	2.9	2.9	4.1
Dodge & Cox Income	DODIX	48.86	0.7	3.7	3.0	3.4	5.0
Vanguard Sh-Tm Bd;ETF	BSV	48.42	0.4	0.7	1.3	1.2	2.9
iShares:Core US Agg Bd	AGG	43.33	0.8	0.8	2.6	2.2	4.2
Templeton Gl Bond;Adv	TGBAX	40.37	–0.6	10.9	2.4	3.7	6.8
Lord Abbett Sh Dur;F	LDLFX	39.46	0.3	3.1	2.1	2.6	N.A.
T Rowe Price New Inc	PRCIX	33.52	0.8	1.1	2.4	2.3	4.5
American Funds Bond;A	ABNDX	32.43	0.8	1.2	2.5	2.3	3.0
Fidelity Str Adv Cre Inc	FPCIX	30.86	0.8	3.0	3.1	3.0	N.A.
Vanguard Int-Tm Bd;ETF	BIV	30.70	1.1	0.7	3.3	2.8	5.4
iShares:iBoxx $IG Corp	LQD	30.60	1.2	2.2	3.7	4.1	5.5
Fidelity US B Id;IP	FXNAX	28.97	0.7	0.7	2.7	2.2	N.A.

Note: For funds with multiple share classes, only the largest is shown. N.A.: Not applicable; fund is too new or data not available

FIGURE 1.1

Investment Company Total Net Assets by Type

Billions of dollars; year-end, 1998–2015

	Mutual funds[1]	Closed-end funds[2]	ETFs[3]	UITs	Total[4]
1998	5,525	156	16	94	5,790
1999	6,846	147	34	92	7,119
2000	6,965	143	66	74	7,247
2001	6,975	141	83	49	7,248
2002	6,383	159	102	36	6,680
2003	7,402	214	151	36	7,803
2004	8,096	253	228	37	8,614
2005	8,891	276	301	41	9,509
2006	10,398	297	423	50	11,168
2007	12,000	312	608	53	12,974
2008	9,621	184	531	29	10,365
2009	11,113	223	777	38	12,151
2010	11,833	238	992	51	13,114
2011	11,632	242	1,048	60	12,983
2012	13,057	264	1,337	72	14,729
2013	15,051	279	1,675	87	17,091
2014	15,875	289	1,974	101	18,240
2015	15,652	261	2,100	94	18,107

[1] Mutual fund data do not include mutual funds that invest primarily in other mutual funds.

[2] Closed-end fund data include preferred share classes.

[3] ETF data prior to 2001 were provided by Strategic Insight Simfund. ETF data include investment companies not registered under the Investment Company Act of 1940 and exclude ETFs that primarily invest in other ETFs.

[4] Total investment company assets include mutual fund holdings of closed-end funds and ETFs.

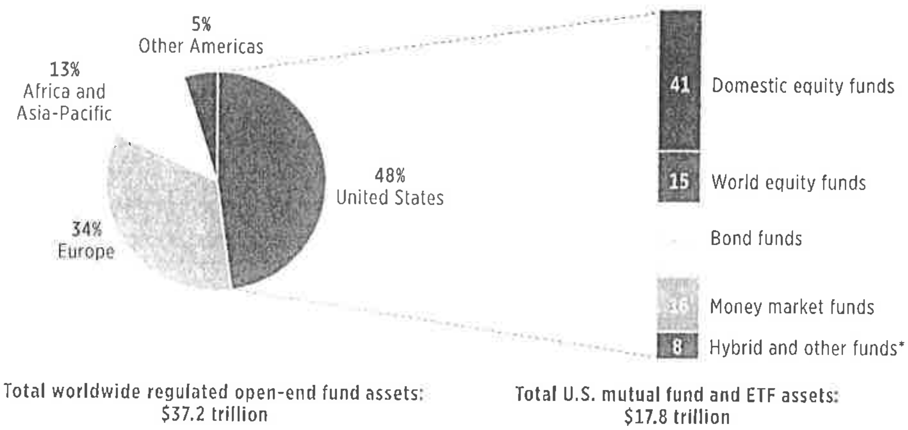
Note: Data are for investment companies that report statistical information to the Investment Company Institute. Assets of these companies are 98 percent of investor assets. Components may not add to the total because of rounding.

Sources: Investment Company Institute and Strategic Insight Simfund

FIGURE 1.2

The United States Has the World's Largest Regulated Open-End Fund Market

Percentage of total net assets, year-end 2015

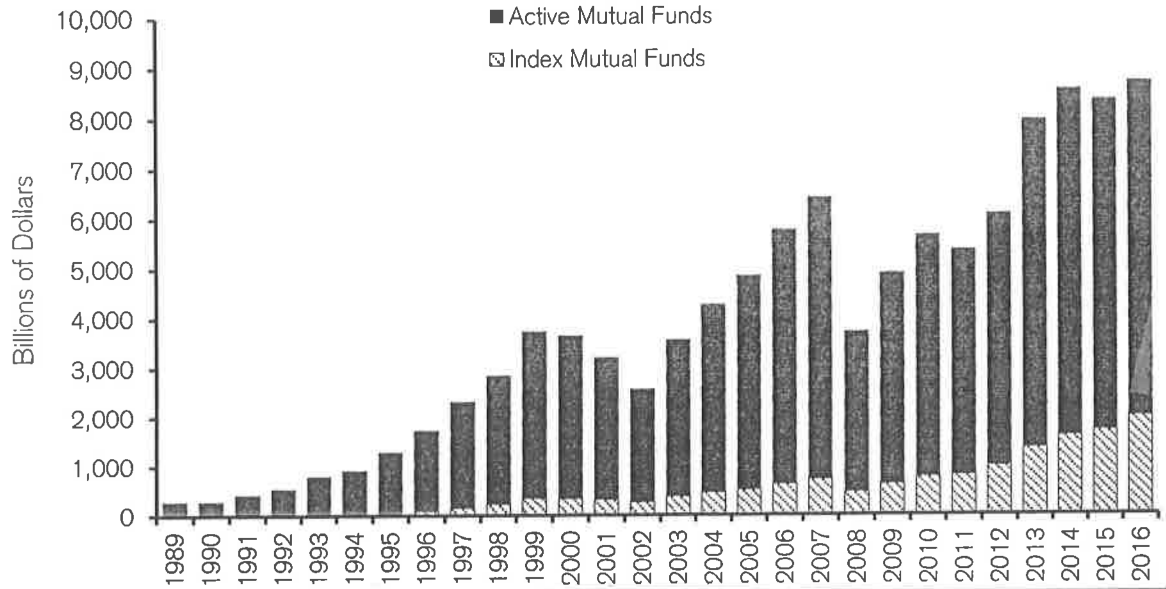


* This category includes ETFs—both registered and not registered under the Investment Company Act of 1940—that invest primarily in commodities, currencies, and futures.

Note: Regulated open-end funds include mutual funds, exchange-traded funds (ETFs), and institutional funds. Components may not add to 100 percent because of rounding.

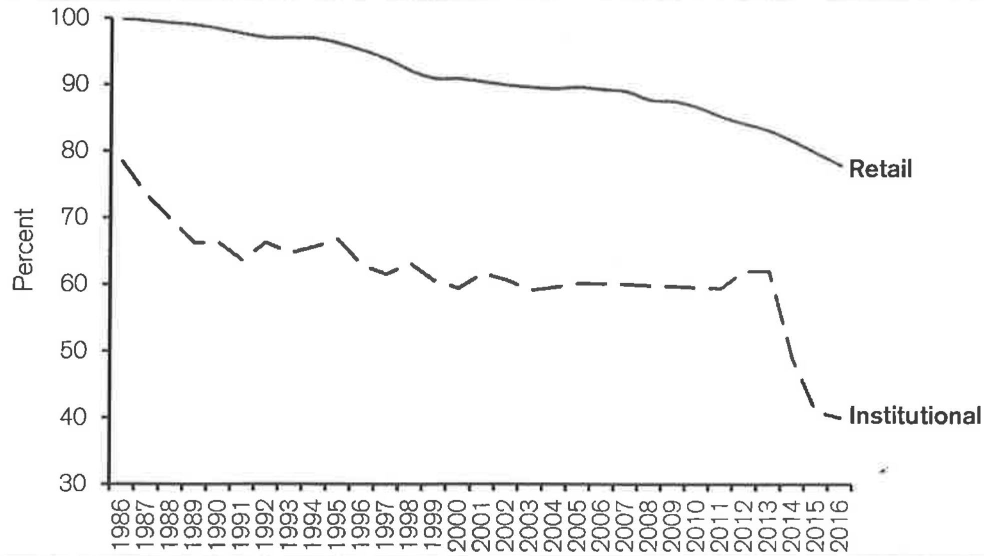
Sources: Investment Company Institute and International Investment Funds Association

Exhibit 5: Assets Under Management of U.S. Domestic Equity Mutual Funds, 1989-2016



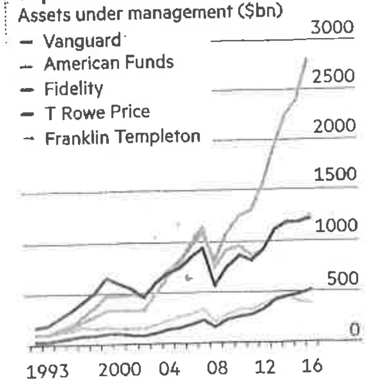
Source: Simfund.
Note: U.S. domiciled equity funds; 2016 figure as of 11/30/16.

Exhibit 7: Active Allocations for Retail and Institutional Investors, U.S. Domestic Equity



Source: Kenneth R. French; Greenwich Associates, "Is There a Future for Active Management? How Active Managers Will Thrive in a Maturing Industry," Q4 2016; Credit Suisse estimates.

Top five US mutual fund families
Assets under management ($bn)



FT March 21, 2017

THE WALL STREET JOURNAL.

Wednesday, December 14, 2016

Active Funds Brainstorm on Outflows

Managers gather to discuss the problem of clients leaving for index-tracking funds

BY SARAH KROUSE

About 60 rival mutual-fund executives gathered inside **OppenheimerFunds**'s Manhattan office tower in early November to discuss a problem many of them can't shake: persistent client withdrawals.

The Nov. 2 summit, dubbed "The Seismic Shift Senior Leadership Forum," was a daylong brainstorming session about the mass movement of investors from money managers that try to beat the market. Clients are flocking to index-tracking funds that offer simplicity, lower fees and the assurance of matching the market.

Some attendees argued that fees have to decline more aggressively if stock and bond pickers are to compete, said people at the meeting. Others advocated for a clearer public message about what they see as the benefits of active management, these people said.

The gathering, prompted by changing industry economics, was unusual because it brought together so many types of executives who compete for clients and assets. Attendees included investing, sales and product-development executives from **T. Rowe Price Group** Inc., **Franklin Resources** Inc., **Affiliated Managers Group** Inc. and **Janus Capital Group** Inc.

Details of the forum, which was hosted by trade group Mutual Fund Education Alliance, haven't been reported previously.

Speakers included OppenheimerFunds Chief Executive Arthur Steinmetz, who spoke to the audience on a small stage. Throughout the day's presentations, a series of panelists sat in wooden director's chairs as slides rolled behind them, addressing rows of attendees seated at long white tables.

Money managers are experimenting with previously unpopular approaches as they grapple with an unprecedented flow of money out the door.

Some firms that focus on active management are ramping up efforts to retain or attract investors through fee waivers or cuts, moves they were reluctant to adopt in years past, or trying for new footholds in passively managed products.

Others are trying to expand overseas or develop funds across new asset classes to bring in higher fees.

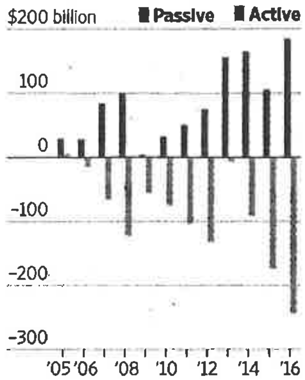
Over the past year, investors have pulled $242.7 billion from funds that bet on U.S. individual stocks, while placing $185.9 billion into U.S. mutual funds and exchange-traded funds that track stock indexes, according to Morningstar.

Revenue growth for the asset-management industry is projected to slow to 2.9% a year between 2015 and 2021. That compares with 6% a year between 2011 and 2015, according to a report published earlier this month by Deloitte's Casey Quirk unit, which focuses on asset management.

Fees also are expected to drop further, the consulting firm said. The average passive stock fund has an asset-weighted annual fee of 0.11%, while the average annual fee for actively managed U.S. stock funds is 0.78%, according to Morningstar.

Moving Out

Estimated net asset flows for U.S. stock mutual funds and ETFs



*Data for 2016 are through November
Source: Morningstar
THE WALL STREET JOURNAL.

Some actively managed firms are rolling out more-aggressive advertising and using public events to make their case. Family-owned active manager **Baron Funds** devoted portions of its New York annual shareholders meeting Nov. 4 to a denunciation of index trackers.

In between performances from Hugh Jackman, comedian Louis C.K., singer Kenny Loggins and the cast of the Broadway play "Hamilton," Baron President Linda Martinson cited the Dutch tulip mania and the dot-com boom as cases in which investors bought and sold at the wrong time. Active managers like Baron, she said, have the ability to sidestep such crashes.

"What you get is mediocrity" with passive investing, she told more than 5,000 shareholders at Lincoln Center. Active management is at the point of "maximum financial opportunity."

Baron didn't attend the Seismic Shift Senior Leadership Forum, but what it has in common with many of those firms is the pattern of client withdrawals in recent years.

The Mutual Fund Education Alliance has convened industry executives in the past but typically in smaller groups. This year it decided to expand the participants because fund executives said industry changes warranted a more-sweeping discussion, according to people familiar with the gathering.

The mutual-fund group discussed how active managers should respond to media coverage on the growth of passive investing, forthcoming regulatory changes from the Labor Department governing retirement advice, and ways to use both active and passive management in investor portfolios, the people said.

What they learned from a private survey is that most of the trade group's members expect the movement away from traditional money managers to persist, the people said.

A consultant from Casey Quirk told them the survey of group members found that two-thirds expect the growth of passive investing to continue at its current rate over the next five years. Of the respondents, 19% said they expect the growth of index-tracking funds to accelerate further.

Some fund houses 'manipulate' benchmarks

MADISON MARRIAGE

The fund industry has been dealt a damaging blow by its own professional body. It has accused asset managers of selecting inappropriate benchmarks in a bid to market themselves more easily to investors.

The CFA Society of the UK, a body that provides training to 11,000 investment professionals, said it has found evidence of fund managers "misusing benchmarks to demonstrate that they have skill when, in fact, this can just be an illusion".

In a report issued by the society, it found that poor practices range from selecting and using inappropriate benchmarks to overlooking the impact of leverage.

> 'Some smaller houses will try and paint their performance in as good a light as possible'

Fund groups might be tempted to misuse benchmarks in this way if they are "more interested in asset gathering than in delivering performance to clients", said Will Goodhart, chief executive of CFA UK.

Jake Moeller, head of UK research at Lipper, the data provider, agreed there was scope for benchmarks to be misused.

"Benchmarking can certainly be manipulated if the fund manager nominates a benchmark that makes them look good in a certain sector. That is a problem," he said. "Some smaller houses will try and paint their performance in as good a light as possible when they want to get assets."

An asset manager could nominate a large-company stock index as their benchmark, for example, but primarily invest in mid-sized companies, Mr Moeller said. This could unfairly flatter their performance.

Mr Moeller said it was unlikely that "reputable" fund houses engaged in such practices. "I do not think fund groups are that cynical. Most fund managers work on a best-practice basis and reputable fund groups do not want to be seen to be manipulating benchmarks," he said.

THE WALL STREET JOURNAL.
WSJ.com

MUTUAL FUNDS | AUGUST 9, 2010

Low Fees Outshine Fund Star System

By JANE J. KIM

Low fees are likely to be the best predictor of a mutual fund's future success, according to a new study by Morningstar Inc.

The study, to be released Monday, shows that using low fees as a guide would give investors better results than even Morningstar's own star-rating system, which looks at past risk- and load-adjusted returns. While the stars system has typically guided investors to better results, it isn't as effective in predicting future returns at times of big market swings.

Morningstar found that in aggregate, low-cost funds had better returns than high-cost funds across all asset classes, during various periods from 2005 through March 2010.

Fees "have proven to be the strongest predictor out there." says Russel Kinnel, director of fund research and author of the study. "The stars system, as a measure of past risk-adjusted performance, is going to be a little more limited."

For example, domestic stock funds in the cheapest quintile in 2005 posted average annualized returns of 3.35% over the ensuing five years, compared with average returns of 2.02% for funds in the most expensive quintile, according to the study.

Under Morningstar's ratings system, five-star funds generally beat one-star funds.

There were exceptions. Five-star international stock funds posted lower average annualized total returns than one -star funds from 2005 through March 2010.

One reason: Many of the one-star funds were closed during that period, so their returns weren't factored in, while the surviving one-star funds generally had taken bigger risks, reaping higher total returns.

Only 74 of the 146 one-star international stock funds in 2005 survived the ensuing five years; of that group, only 19 outperformed peers during that period.

When fund companies close or liquidate mutual funds—generally high-cost or one-star funds—they can essentially sweep mistakes under the rug. "There really is a huge cycle of destruction in the fund world," Mr. Kinnel says. "If you only look at the funds that still exist, you significantly understate how important that is."

C2 | Wednesday, November 16, 2011 THE WALL STREET JOURNAL.

Morningstar's New Planet

Updated Ranking System Tries to Predict Fund Performance, but Stars Remain

BY JOE LIGHT

Investment-research firm **Morningstar** Inc. on Tuesday unveiled a forward-looking ranking system for mutual funds to supplement the company's closely watched one- to five-star ratings.

Chicago-based Morningstar says the new system—which grants funds a gold, silver, bronze, neutral or negative ranking—is meant to predict which funds will outperform their peers in the future.

By contrast, the star ratings are granted based on past performance after adjusting for risk and sales charges. The stars are widely used by investors and financial advisers in choosing funds to buy and often are touted in promotional materials.

The new ratings are based in part on past performance, but also employ other quantitative and qualitative measures including the fund's expense ratio, Morningstar's perception of the fund manager, the fund's parent company and the fund's investment strategy.

Of the 349 funds that Morningstar already has rated under the new system, 155 achieved the highest "gold" rating, while eight received a "negative" rating.

The company initially focused on larger funds and ones that it had formerly deemed "analyst picks," said Russel Kinnel, Morningstar's director of fund research. It expects that the balance of negative and positive ratings will become more even over time.

The **Wells Fargo Advantage Ultra Short-Term Income** fund, which is rated four stars under the old system, received one of the negative ratings under the new one.

"We believe in the management team's investment process and have comfort in their credit analysis and risk-management capabilities," a Wells Fargo spokesman said in a statement.

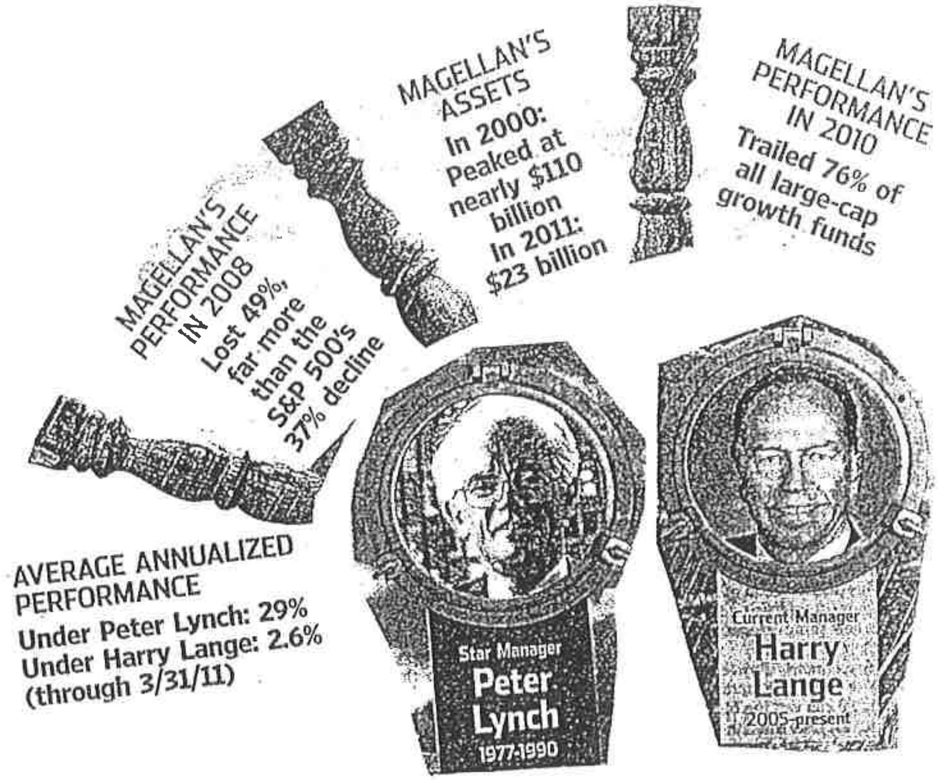
On the other hand, the **Clipper Fund**, which has one star, earned a gold designation.

If the new ratings catch on, the implications for fund managers could be significant. More than 122% of mutual-fund inflows over the last five years have gone into funds that are now rated four or five stars, according to Morningstar. The number is greater than 100% because one-, two- and three-star funds have seen net outflows over that period.

"We still get calls that say, 'Hey, why haven't you gotten me out of this two-star fund?'" said Tim Courtney, chief investment officer of Oklahoma City-based wealth manager Burns Advisory Group Corp.

Mr. Courtney said there was a widespread misperception among investors that the star ratings were meant to indicate a fund's quality, and that he hopes the new system will help change that.

THE WALL STREET JOURNAL. *Saturday/Sunday, April 23 - 24, 2011*



MORNINGSTAR FUND RATINGS

★★★★★ December 1985

★★★★ September 1992

★★★ April 1996

★★ June 2004

★ November 2008

'Six months from now, I'll look like I'm a star.'

-Fidelity Magellan manager Harry Lange, in April 2011

'Harry will ... explore other opportunities within the company that leverage his investment management talent and experience.'

-Fidelity spokesman Vin Loporchio, on Tuesday

THE WALL STREET JOURNAL. *Wednesday, September 14, 2011*

Miller Spies Value In Valeant Shares

BY JASON ZWEIG

MUTUAL FUNDS

Not every value investor bought **Valeant Pharmaceuticals International** Inc. high.

Bill Miller, manager of the $2 billion **Legg Mason Opportunity Trust**, says he sank about 3.5% of the fund into Valeant in late March and early April, mostly at prices between $28 and $32 a share. Valeant closed at $36.23 Tuesday.

Mr. Miller rose to fame between 1991 and 2005, when the fund he then managed, Legg Mason Value Trust, achieved the unparalleled feat of outperforming the S&P 500 for 15 years in a row. His trademark was perceiving undervaluation where others saw overpricing—as in Amazon.com Inc. during the Internet bubble, Tyco International PLC after its accounting scandal and Alphabet Inc. (then known as Google) in its initial public offering.

The fund peaked at more than $20 billion in 2007. But Mr. Miller, by his own admission, stuck too long with financial stocks such as Bear Stearns Cos. and American International Group Inc. Legg Mason Value Trust (since rechristened ClearBridge Value Trust) lost a dreadful 55% in 2008, and Mr. Miller stepped aside in 2011.

Since 2000, Mr. Miller has run the smaller Legg Mason Opportunity Trust, where he has amassed big positions in home builders, airlines and other unorthodox picks.

This fund, too, has been like the girl who had a little curl: When it is good, it is very good indeed, as in 2012 and 2013, when it gained 41.1% and 68.4%, outperforming the S&P 500 by 16 and 32 percentage points, respectively. And when it is bad, it is horrid, as it was in the first quarter, when it underperformed by more than 12 percentage points. Overall, since its launch, the fund has beaten the market by an average of more than half a percentage point annually.

"We like to buy companies that can earn above the cost of capital for long periods of time, especially after they have been annihilated and we can keep them for years," he says.

Valeant is under investigation by the Securities and Exchange Commission and other authorities amid allegations of accounting irregularities; the company has identified misstatements in some of its 2014 and early 2015 reports and delayed the filing of its 2015 year-end financial statements.

Mr. Miller is gambling that Valeant's accounting problems are mostly behind it and that, at recent prices, the underlying businesses still are worth owning.

Mr. Miller reckons that Valeant's operations, including its Bausch & Lomb, Salix and Medicis units, should generate about $7 a share in free cash flow this year and perhaps $9 next year.

"It wouldn't surprise me if revenues were disappointing relative to guidance over the next quarter or so," he says. "Sales could well drop off temporarily because of all the bad publicity. But the totality of these businesses aren't in dying assets."

Valeant, Mr. Miller says, is "in this chasm right now where almost all the news is bad, and the news flow isn't going to make anybody jump up and down for joy anytime soon."

Without even a current financial statement to go on, Valeant is "like a poster child for every aspect of behavioral finance," he says, as investors focus their attention on what already has gone wrong and what else could still go wrong.

"The normal contrarian buyers just aren't there anymore," he says. "Nobody wants to own Valeant except for people like me who've been around for so long."

Many of his fund's board of directors have known him for decades, Mr. Miller says: "They've seen this movie before, and they're comfortable with the strategy."

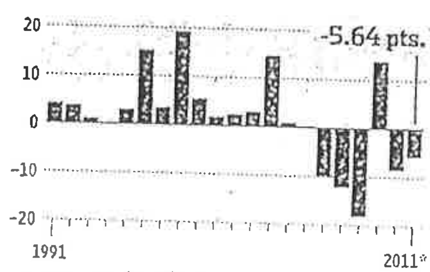
As so often has been the case, Mr. Miller isn't likely to be proved half-right. He will either hit a home run with Valeant or strike out.

"Where you want to take some risk," he says, "is on companies that have already gotten crushed."

RICK SCIBELLI JR. FOR THE WALL STREET JOURNAL

'Nobody wants to own Valeant except for people like me,' says Bill Miller, manager of Legg Mason Opportunity Trust, shown in 2014.

Fund total return vs. S&P 500 total return (percentage points)



* Year-to-date

WSJ 11/18/2011

From 1991 to 2005, Mr Miller beat the US stock market every year in an unmatched 15-year run at the head of Legg Mason's flagship mutual fund.

The financial crisis was unkind, however, and when in late 2011 he announced he would step down from the fund, it was the worst performer over five years, behind more than 800 peers, according to Lipper, a research group.

FT Feb 6, 2013

Active Managers Stage a Comeback

By Justin Baer and Sarah Krouse

THE WALL STREET JOURNAL.

Bill Miller is on a winning streak again.

His $1.4 billion Miller Opportunity Trust is up 7.5% so far this year and has climbed 21% in the past 12 months, according to Morningstar. Its performance this past year has been helped in part by its holdings of bank stocks including **Bank of America Corp.** and **J.P. Morgan Chase & Co.**

MARKETS REVIEW

Mr. Miller isn't alone: Some 45% of all U.S.-based actively managed stock, bond and other mutual funds were beating their benchmark indexes as of Feb. 28, Morningstar said.

Helping these managers is a market rally that has rewarded bets on companies expected to benefit the most from a strengthening economy. The Trump administration's promises of lower taxes and fewer regulations have helped lift business confidence and pushed stocks higher.

Some investors are optimistic that conditions are right for active managers' resurgence to continue, eventually slowing the flow of money out of actively managed funds into lower-cost index-tracking funds, a trend that has hounded many of them in recent years.

"Active managers are getting a little more confidence, and maybe reaching out a bit more," said Mr. Miller, a former star manager at Legg Mason who posted an unparalleled 15-year winning streak against the market that ended in 2006.

To be sure, the rally does little to make up a lengthy stretch of underperformance for these money managers. The last year when even half of all active funds beat their benchmarks was 2009, according to Morningstar. In 2016, 31% of actively managed funds beat their benchmarks.

But the recent rebound has helped. Actively managed mutual funds in February posted their first month of positive net inflows since April 2015, according to Morningstar. Those were helped by money flowing into bond funds as well as international stock funds.

Monday, April 3, 2017

LUBOS – FYI.
Allan Friedman

THE NEW YORK TIMES, SUNDAY, JANUARY 5, 2003

MARK HULBERT

Weighing Means, Not Just Ends, to Rate Fund Managers

THREE finance professors have devised a new mutual fund rating system that appears to do a better job of separating managers whose performance reflects genuine ability from those whose results depend on luck alone.

At its core, the new system assumes that a manager's ability can be detected by comparing his portfolio with those of other fund managers — and not by looking at his own past performance. If the stocks he currently owns are also owned by managers with stellar records, for example, then the odds are high that he is a good manager. In contrast, he probably is not worth betting on if he holds only stocks that are primarily owned by managers with awful records.

The idea is a significant departure from traditional approaches to rating mutual funds. Under the new system, a fund with a dismal record may receive a high rating, provided that its current holdings overlap with those of portfolios with good records.

The ratings system of Morningstar Inc. is similar in some ways, because it judges a fund's record in comparison to other funds that have a similar style. But unlike the new system, Morningstar's would never give a higher rating to a fund whose performance was inferior to others in its category.

The authors of the research, Randolph B. Cohen and Joshua D. Coval of the Harvard Business School and Lubos Pastor of the University of Chicago Graduate School of Business, use a basketball analogy to illustrate their reasoning. Imagine a 10-shot free-throw contest between two players, one who shoots with one hand and the other who shoots with both hands. Which player would you bet on if, at the halfway mark, both players had made all five of their shots?

If you rate basketball players by their records, you have no preference. But what if you find that, across the league, two-handed shooters make a much higher percentage of their free throws? The intelligent bet would then be on the two-handed shooter, because luck probably played a larger role in the one-handed shooter's good record.

In other words, technique matters. Yet current systems focus on results alone. They overlook a wealth of information that can give insight into managers' ability.

To show how much technique matters, the three professors constructed an elaborate rating system in which a fund's score is a function of the track records of all other funds that hold any of the same stocks. The highest-rated funds will be those whose stocks are primarily owned by market-beaters, while the lowest-rated will hold stocks that are mostly owned by losing funds.

The new system is superior in two ways to approaches that focus only on results. First, there is a higher degree of statistical confidence in its conclusions — from four to eight times higher, according to the professors, depending on how those traditional approaches adjust performance for risk.

Consider funds that have been around for less than five years — a group that, according to Lipper Inc., now contains 55 percent of all United States diversified and sector equity funds. According to Professor Cohen, a focus on track records alone for such funds "can be quite misleading" because there is not enough data to have much confidence that winning managers have genuine ability or that losers were not just unlucky.

The professors largely sidestep this difficulty. Even a young fund typically owns several dozen stocks, providing many data points. Generally, confidence levels increase as more data becomes available.

The second advantage of the new system is its better ability to identify funds that will outperform the market. Had this system been used from April 1977 to December 2000, investors who followed it would have made as much as 1 percent more per year than they would have by relying on ratings systems that focus on track records alone.

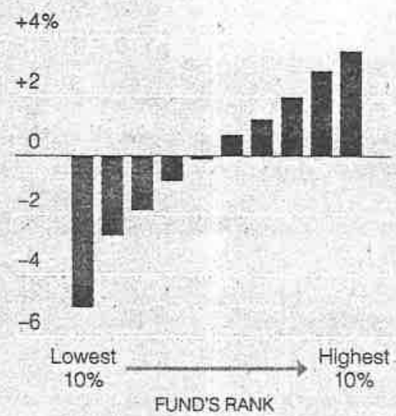
Though this new research has not yet been published, it has been the subject of nearly a dozen graduate school seminars over the last few months. It is available at http://ssrn.com/abstract_id=353620.

One early criticism concerned the professors' treatment of window-dressing — the end-of-the-quarter tendency to buy stocks that have performed the best during the quarter and to sell losers. Window-dressing makes managers look like shrewd stock pickers. Wouldn't the new system erroneously conclude that such managers have great ability, because their portfolios now hold stocks that are owned by top-performing funds?

According to Plan

A new mutual fund rating system compares each fund with all other funds that own any of its stocks. In tests based on historical data, funds rated most highly by this system outperformed the market, while those rated at the bottom underperformed.

FUND PERFORMANCE RELATIVE TO STOCK MARKET*



*Based on quarterly application of this rating system from April 1977 to December 2000 and a value-weighted composite of the entire United States stock market.

Sources: Profs. Randolph B. Cohen, Joshua D. Coval and Lubos Pastor

The New York Times

In response, the professors modified their system, so that it now also looks at when a manager buys or sells. It gives a higher score to a manager whose timing of transactions more closely matches that of other managers with good track records.

To be sure, funds do not divulge the precise dates on which they buy or sell stocks. But one can get a good idea by comparing their end-of-the-quarter reports.

But how can the new system accurately rate an innovative manager — one whose stocks are not held by any other fund? To return to the basketball analogy, imagine that one of the two contestants in the free-throw contest was Rick Barry, who was famous in the 1960's and 70's for his unique underhand free-throw technique and for having one of the higher free-throw percentages in professional basketball. Since there were too few other professional players with whom to compare his technique, how could the professors' system recognize his abilities?

THE professors do not deny the theoretical possibility of a Rick Barry in the mutual fund arena. But they do minimize the probability. According to Lipper, there are 6,843 United States diversified or sector equity mutual funds, more than twice the number of publicly traded American companies with market capitalizations of at least $100 million. Because the average fund owns several dozen stocks, the odds are very small that none of a fund's stocks will be owned by any other fund.

The professors do not yet know the answer to one question: Can their rating system be improved further by combining it with more traditional approaches? Consider two funds that hold stocks that are also owned by top-performing funds. Is the one that has made the most money a better bet for future performance? Professor Cohen says research on that issue is just beginning.

Unfortunately, the mathematics and data needed to replicate the professors' new system are beyond most individual investors' capabilities. Our best hope of taking advantage of this new research is that a major fund rating service will incorporate it. □

Mark Hulbert is editor of The Hulbert Financial Digest, a newsletter based in Annandale, Va. His column on investment strategies appears every other week. E-mail: strategy@nytimes.com.

Goldman offers ETF linked to hedge data

Asset management arm hopes to capitalise on closely watched research

MARY CHILDS — NEW YORK

Goldman Sachs is seeking to capitalise on its most popular research publication by offering an exchange-traded fund based on its data on hedge fund positions.

Many investors scrutinise the US bank's Very Important Positions index and use it as a window on to what hedge funds are doing. The index highlights the 10 stock bets that appear most frequently among bullish plays in hedge fund portfolios.

The GS Hedge Industry VIP ETF will track those data, giving investors an easy way to put their money into the same bets.

The ETF began trading on the NYSE Arca yesterday with $20m. It will charge 45 basis points, compared with an industry average of about 35bp, according to an Evercore ISI report.

However, scepticism about hedge funds has been growing. Some big pension funds are cutting their exposure and returns have lagged behind the broader markets.

Hedge Fund Research's asset-weighted index returned 0.5 per cent to the end of September, compared with 2.6 per cent for the S&P 500. The industry is often criticised for "idea overlap", with multiple funds piling into the same "hedge fund hotels".

Goldman Sachs Asset Management started offering ETFs in September last year and has seven funds, which combined had about $2.5bn in assets at the end of last month. These funds are dedicated to so-called smart beta strategies, which invest according to certain set factors.

The ETF market as a whole has ballooned to $3.3tn in assets, according to data provider ETFGI, as investors have piled into low-cost offerings that track indices.

HFR said last month it aimed to start the first futures contract on a hedge fund index, in partnership with a derivatives exchange. It is in talks with industry participants to gauge likely interest.

The GS Hedge Industry VIP product combines the ETF structure with popular enthusiasm for products that focus on high-conviction ideas.

> VIP product comes at a time when scepticism about the sector is growing

Credit Suisse Asset Management said it was starting a "best ideas" fund out of its fund of funds business this year, and KKR has similar vehicles.

At the same time, "crowding" has been cited as a top concern among hedge funds and their investors. With more participants, better technology and declining liquidity, uncorrelated returns have become more difficult to generate.

While crowding can be a successful strategy in rising markets, "when the reverse happens, it tends to be sharp and painful", according to a report from Barclays' capital introductions group.

See Lex

UPSIDE | By Brett Arends

Saturday/Sunday, October 20 - 21, 2012

It's Time to Time the Market

THE WALL STREET JOURNAL.

Trying to "time" the market is risky. But as stocks and bonds sit near record highs, investors might want to consider some version of it.

Merely to suggest market-timing is to reject generations of advice. "Don't try it—ever," warned Charles Ellis in his investment classic "Winning the Loser's Game," calling it a "wicked" idea.

John Bogle, founder of Vanguard Group, noted in his book "Common Sense on Mutual Funds" that "after nearly 50 years in this business, I do not know of anybody who has done it successfully and consistently...I don't even know of anybody who knows anybody who has done it successfully and consistently."

Studies show that most investors who try to time the markets fail, buying high and selling low. Yet it is possible to glean meaningful clues from current indicators—and tweak portfolios for the longer term.

Which brings us to today. U.S. Treasurys and stocks seem expensive by historical standards. To stay fully invested is to risk mediocre returns.

Treasury bonds are almost certain to lose. Ten-year Treasurys boast a yield of just 1.8%, while the bond market is forecasting inflation of about 2.5%, based on the difference in yields between inflation-adjusted and regular Treasurys. If that plays out, a Treasury investor will have less purchasing power in 10 years—a de facto loss.

Over the past 80 years, according to data from New York University's Stern School of Business, bond investors have earned an average of just over 2% a year, adjusted for inflation. The only way an investor would earn anything similar over the next decade would be if inflation were negative.

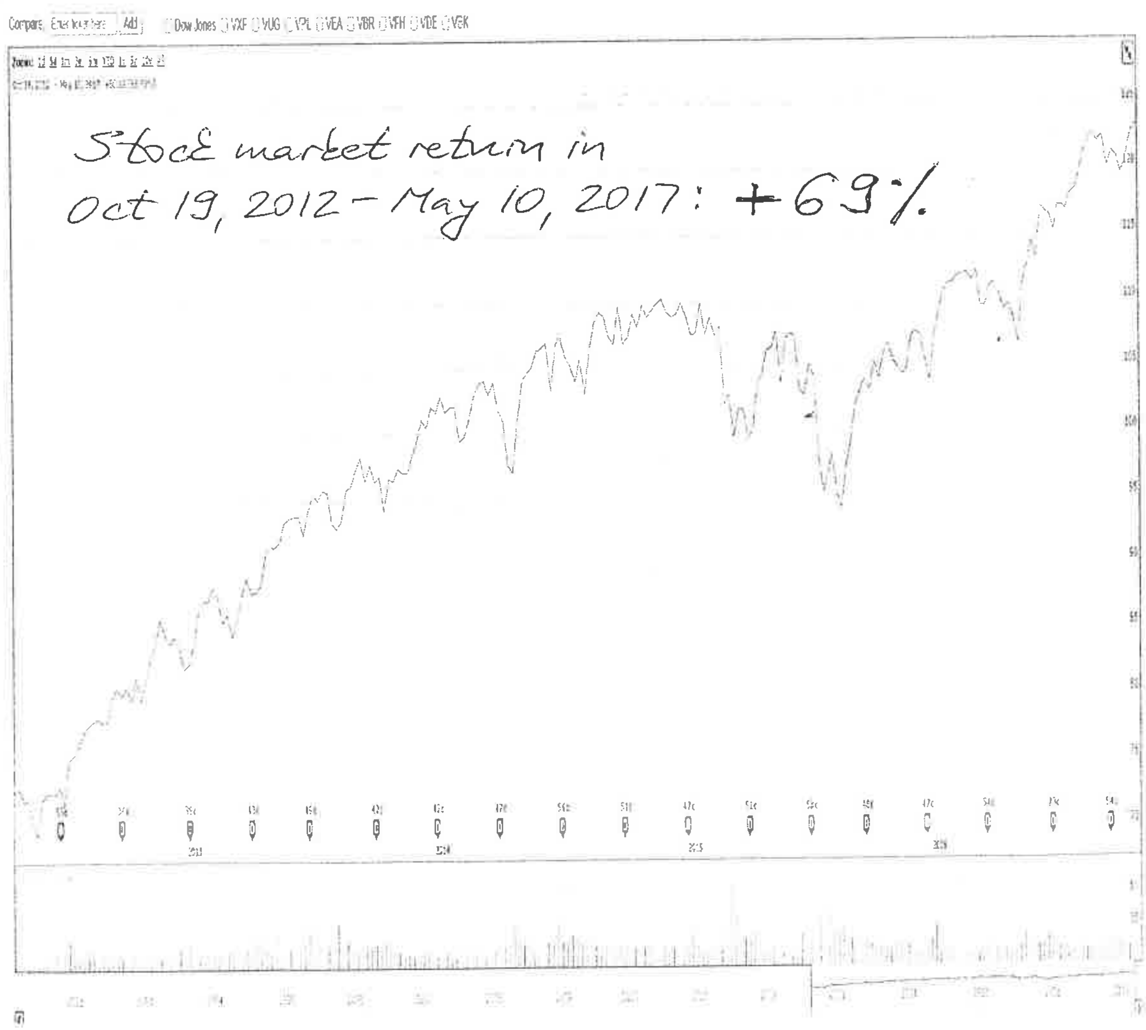
Stocks, too, seem pricey. Over the past 130 years, U.S. stocks on average have traded at about 17 times mean earnings for the previous 10 years—a measure known as the "Shiller Price/Earnings Ratio" after Yale economics professor Robert Shiller, who tracks the data. Today the market is about 22 times those earnings, a level associated with frothy markets such as 1929, the mid-1960s,

[redacted]

and most of the period from 1995 to 2008.

Another measure, "Tobin's q," also suggests stocks might be in dangerous territory. Tobin's q, named for the late Nobel economics laureate James Tobin, measures stock valuations against the cost of replacing companies' assets. Right now the reading is 0.92, about 50% above the long-term historical average. Stock returns from these levels have usually been subpar.

"Equities and bonds in America are seriously overvalued," says Andrew Smithers, chairman of London-based financial consultancy Smithers & Co. Fund company GMO, with $100 billion under management, predicts meager returns over the next seven years from U.S. bonds and most U.S. stocks.



An ETF Built to Time the Market

Blair Hull has created an ETF based on research showing that market signals can predict market moves.

By CHRIS DIETERICH
May 28, 2016

Barron's

This year has proved humbling for prognosticators. British soccer club Leicester City, given 5,000-1 odds to win its league, clinched the title. Bookmakers at one point last summer gave Donald Trump 80-1 odds to seal the Republican presidential nomination.

Add another unlikely candidate for beating the odds: Blair Hull, a mathematician and electronic trading pioneer whose $45 million Hull Tactical US exchange-traded fund (ticker: HTUS) debuted last June. He claims to predict the future with the trading equivalent of reading tea leaves—the Baltic Dry Index of sea-shipping rates.

ETFs by Category ›

Hull, who cut his teeth counting cards from Reno to Lake Tahoe in the 1970s, made his name as a renowned trader in the 1987 crash, when he correctly called the market bottom. His firm, Hull Trading, was launched in 1985 based on an options-pricing model he had developed a decade earlier, and staffed with physicists and computer scientists in the early days of computerized trading. It operated in nine countries when it was purchased by Goldman Sachs in 1999. Hull later founded Ketchum Trading, an elite electronic trading firm, and has dabbled in politics. (He was defeated in the Illinois Democratic primary for U.S. Senate in 2004 by Barack Obama.) Hull, 73, looks every bit the politician, with straight silver hair and rimless glasses, but admits to being more suited to science than art.

For instance, when a *Barron's* columnist accidentally referenced his poker-playing history, Hull quickly interjected: "It was blackjack, not poker. There's a big difference. In poker, you've got to be able to read people and bluff—neither of which I do very well."

HULL'S MOST RECENT OBSESSION has become predicting market outcomes. A paper he and a colleague published last year found that blending 20 market signals—including the aforementioned Baltic Dry Index, short interest, moving average, and other more-esoteric measures—can reliably forecast where U.S. stocks are headed on the whole six months into the future. This research is the basis for the ETF, which can dial up or down positions in Standard & Poor's 500 index futures or the SPDR S&P 500 ETF (SPY) each day based on market-return forecasts.

Hull tells investors to expect outperformance in two out of every three years, and posts a quiz to test "general knowledge of return predictability" on his Website that he encourages investors to take before investing. There's more to consider: Frequent trading makes the ETF a poor fit for taxable accounts; investors would do better to own this inside an IRA. Expenses are high but far less than hedge fund strategies; at 0.91%, fees are slightly lower than the largest alternative ETF on the market, the $1.1 billion IQ Hedge Multi-

Enlarge Image

An unlikely candidate for beating the odds: Blair Hull, a mathematician and electronic trading pioneer whose $45 million Hull Tactical US ETF debuted last June. *Photo: Bloomberg News*

Strategy Tracker (QAI), which charges 0.97%.

In some ways, this opaque-sounding strategy is relatively transparent. Daily forecasts from the predictive indicators are published on Hull's website, and enterprising investors could trade off his information on their own. The strategy will evolve over time, Hull says. In November, the ETF tweaked its strategy to incorporate predictions of one-day stock price moves; in its current configuration, positions are based on one-day and six-month forecasts.

As of Thursday, for instance, Hull's cryptic model, which is currently favoring "Proprietary Variable X," indicates that stocks are likely to be down six months from now, but up in the next few days. The ETF, which can be 200% long or 100% short, adjusts its exposure to the S&P accordingly.

WHILE THE STRATEGY IS COMPLEX, Hull says the aim is to beat the market but also enhance risk-adjusted returns. Simulations in his academic paper show annualized returns double that of the market, and a Sharpe Ratio four times as large, indicating one-quarter of the risk. This year's trading shows how that can work. The ETF's median daily price move this year is just 0.03%. It plods along when signals are mixed, but should bound higher when the coast is clear.

The strategy has returned 3.9% since its June inception, versus 1.2% for the S&P 500 in the same period, according to Morningstar.

This ETF is clearly not for everybody. Hull even acknowledges it's essentially a pet project he created for friends to invest in what he considers to be the next frontier—the interplay between the flood of new and readily accessible sources of data and cutting-edge advances in the field of statistical learning.

"It's been ingrained that timing the market is a bad idea," he says. "The combination of data and predictive analytics, these two tools, can make it possible." Hull contends that market-timing models could eventually become as commonplace as index funds. Any stigma, he says, will fade as the machines prove their worth: "Just as in the past 30 years it's been considered irresponsible to time the market, in the next 30 years it will be considered irresponsible not to time the market."

Active fund managers 'growing too big'

AllianceBernstein chief says size is coming at the expense of performance

ROBIN WIGGLESWORTH
US MARKETS EDITOR

The asset management industry has grown too bloated to produce consistently market-beating returns and needs to be more disciplined on size to restore investor faith, according to the head of one of the biggest US investment houses.

Money has gushed out of traditional stockpicking funds in recent years and into cheap "passive" strategies such as exchange traded funds, as portfolio managers have proved increasingly unable to beat benchmarks after fees.

Last year stock ETFs attracted nearly $200bn while actively managed equity funds suffered $124bn of outflows. Bond funds too are succumbing to the slow but sure exodus to ETFs, reversing some of the huge inflows in recent years.

Peter Kraus, chief executive of AllianceBernstein, a $479bn New York-based asset manager, said in an interview with the Financial Times that funds had to take part of the blame for their deteriorating ability to beat the market. "There is a scale problem in the industry," he said.

Once a mutual fund reached a certain size "the incentives shift from trying to outperform your benchmark to not wanting to underperform", he said.

"Our advice to the industry is to constrain ourselves. We are hurting ourselves by growing too big."

AllianceBernstein was hit by a wave of withdrawals after the financial crisis and, as part of a turnround plan, Mr Kraus has introduced "capacity" caps on funds to ensure that size does not come at the expense of performance.

In 2014 the investment manager closed its Select US Equity fund, managed by Kurt Feuerman, a former senior managing director at the Caxton Associates hedge fund, when it hit its $15bn capacity, and last year closed its $1.5bn European Opportunities Fund to new investment.

The money management industry was in "secular decline because it has overcapacity", Mr Kraus said. "We're just going to where we see the puck going."

Both the swelling size and proliferation of fund managers are weighing on the returns of active management, according to Mr Kraus. The number of US mutual funds had more than doubled in two decades to more than 9,000, but "intuitively the number of talented managers hasn't doubled", he said.

$124bn
Outflows suffered by active funds last year, as stock ETFs attracted nearly $200bn

9,000
Number of US mutual funds, more than twice the figure two decades ago

"If there are no capacity constraints, the returns would be constant with assets under management, but we know that's not true. You end up buying more stocks with low conviction."

However, Mr Kraus expressed wariness over the swelling universe of ETFs. Investors scarred by the underperformance of their money managers — and captivated by the liquidity of ETFs — were herding unthinkingly into another set of risks, he said.

"There is probably too much money in the world today for active . . . But people are making the illogical leap that they should put all their money into passive," said Mr Kraus.

"If people realised the risks around ETFs the behaviour would be much more moderate."

THE WALL STREET JOURNAL. Saturday/Sunday, February 22 - 23, 2014

HULBERT ON INVESTING | By Mark Hulbert

Why New Funds Are Better

Looking to rejuvenate your stock portfolio? Mutual funds that are only a couple of years old are more likely to beat the market than those that have been around for a decade or more.

That is the provocative conclusion of a study released this month by finance professors Lubos Pastor of the University of Chicago's Booth School of Business and Robert Stambaugh and Lucian Taylor of the University of Pennsylvania's Wharton School. It was published by the National Bureau of Economic Research in Cambridge, Mass., a nonprofit group that also officially dates the beginning and end of U.S. recessions.

This new study doesn't mean you should now ignore all other factors that previously have been found useful when choosing a fund, such as recent performance and expenses. But it does mean that when weighing two funds you otherwise find equally attractive, you should go with the younger one, Mr. Pastor says.

The study didn't find a specific age threshold that separated "old" and "young" funds; instead, it found that performance declines steadily and consistently as funds get older.

The researchers focused on actively managed U.S. stock mutual funds between 1979 and 2011—a total of more than 3,000 individual funds—and compared each fund to an appropriate benchmark.

For example, a so-called small-cap value fund was compared with a small-cap value benchmark, while a large-cap growth fund was compared with an index of stocks in that style category.

They found that, when funds were less than three years old, they beat their respective benchmarks by significantly more than funds that were 10 or more years old beat theirs—by an average of about one percentage point a year more, in fact.

While the average fund between three and six years old did less well than those even younger, they still did better than the oldest funds.

Not only is that one percentage point statistically significant, Mr. Pastor says, it also could make a huge difference to an investor over the long term. "Even relatively small return differences should be of interest to investors in today's low-rate environment," he says.

Newer funds have a competitive advantage, Mr. Pastor says, because they are more likely to pursue the latest strategies, which have a better chance of beating the market. By contrast, the strategies that long-established funds began using many years ago may have lost their edge as they are adopted by a lot of other managers.

Younger funds have a competitive advantage because they are more likely to pursue the latest strategies.

"My M.B.A. students who will be fortunate enough to manage a mutual fund will have the benefit of the latest academic research into what works in the market," Mr. Pastor says. "The mutual fund managers who got their M.B.A.s several decades ago were taught what was the cutting edge then, but the cutting edge has moved up a lot since then."

Scott Pollack

A manager who got his M.B.A. in the 1980s, for example, was taught he could beat the market only by investing in risky small-cap stocks or stocks with low ratios of price-to-book value, a measure of net worth. Since then, Mr. Pastor points out, "academia has identified many other potential ways to beat the market, such as by following strategies based on accruals, momentum or stock profitability"—even though, needless to say, there is no guarantee that these new strategies will always work.

Furthermore, he says, today's M.B.A. students are learning many complex econometric tools that weren't available a few decades ago.

Why can't the older managers take advantage of the same latest research as the younger managers? They can, and some do, Mr. Pastor says. But he and his co-authors found that, on average, that "isn't strong enough to overcome the additional competition from the new kids showing up with the latest skills."

To be sure, it can be easier to beat the market when there are fewer assets under management, since it then becomes possible to invest in much smaller-cap companies without adversely affecting their stock prices. Similarly, newer mutual funds don't suffer under the dead weight of the legacy positions that older funds bought in years past—which may not deserve to be sold but yet wouldn't be bought today by a fund starting out fresh.

Yet Mr. Pastor says that this can't explain his and his co-researchers' results: The same conclusions emerged even after controlling for fund size.

Would a younger manager be more likely to incur huge risks in his newer fund in the hopes of making a name for himself? The evidence doesn't seem to support this concern.

Glenn Ellison, an economics professor at the Massachusetts Institute of Technology who also has studied mutual-fund performance, says that—with the possible exception of the tiniest mutual funds—younger managers actually tend to be more conservative than older ones. One big reason, he

Please turn to page B10

Continued from page B7

says: They are much more likely to be terminated for poor performance than an older manager.

Each of the following seven mutual funds can be invested in without any sales charge and has a minimum initial investment of no more than $3,500, at least $15 million in assets and an expense ratio of no more than 1.5%, or $150 per $10,000 invested.

HULBERT ON INVESTING

Among all funds that meet these criteria, according to Lipper, these seven are those with the best 12-month returns—each gaining in excess of 30% over the past 12 months, versus the S&P 500's dividend-adjusted return of 22%.

The first two—**Columbia Active Portfolios Multi-Manager Growth** and **RiverPark Large Growth**—focus on large-cap growth stocks, or those of the largest companies that trade for relatively high price/book ratios. The third, **Lyrical US Value Equity**, also focuses on large-cap stocks, but doesn't confine itself to just growth stocks. A fourth fund, **ASTON/LMCG Small Cap Growth**, falls in the small-cap growth category, while the remaining three are midcap growth funds, which means they focus on growth stocks of midsize companies: **Christopher Weil & Co. Core Investment**, **TCW SMID Cap Growth** and the **Tarkio Fund.**

In addition to showing that younger funds have an advantage over older ones, the new research also illustrates how difficult it is to beat the market. Though today's M.B.A. students will have the latest skills and be the beneficiaries of the latest research, in several years they in turn will be at a competitive disadvantage to the "new M.B.A.s who will be showing up then, who will be at their cutting edge," Mr. Pastor says.

Mark Hulbert is editor of the Hulbert Financial Digest, which is owned by MarketWatch/Dow Jones. Email: mark.hulbert@dowjones.com

Capital Idea #4

Why active fund managers' improving skills don't translate into better performance

Increasing competition makes it harder to beat benchmarks

- Active fund managers' ability to beat benchmarks declines as the industry grows, and improvements in managers' skills don't overcome this effect, according to research by Chicago Booth's **Lubos Pastor,** with Robert F. Stambaugh and Lucian A. Taylor of the Wharton School.

- The researchers measured the impact of both industry size and fund size on an active fund's returns. They controlled for skill, which affects both fund size and performance.

- A $100 million increase in the size of a fund depresses annual returns by two basis points. A percentage point increase in industry size, measured as a fraction of total stock market capitalization, leads to a performance decline of 40 basis points per year for a typical fund.

- Active fund managers have become more skillful in recent decades, especially those in the top percentiles (see chart). However, this has not boosted fund returns because the industry has grown as well.

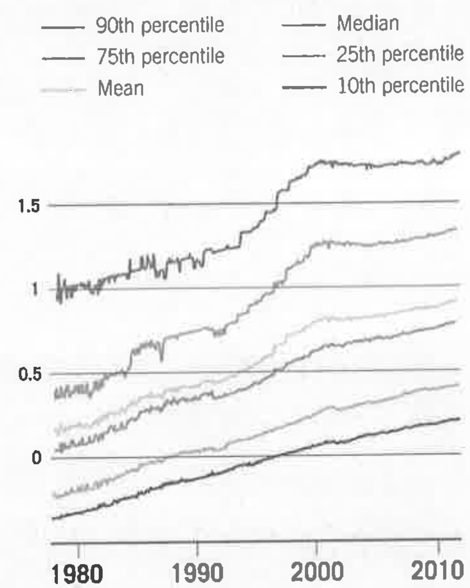
- The researchers define skill as a fund's average benchmark-adjusted return, or alpha, on the first dollar invested. This measures a manager's stock-picking ability before erosion due to the effects of size.

- Younger funds, armed with the latest strategies, are more likely than older funds to beat the market. But their advantage declines as they get older, due to the continued arrival of new competitors.

- The researchers examined data from 3,126 active funds in the United States between 1979 and 2011, a period that saw dramatic growth in the industry.

Upward trend

Estimated skill among active fund managers, % per month



Source: Pastor, Stambaugh, and Taylor, 2014

Younger funds, armed with the latest strategies, are more likely than older funds to beat the market.

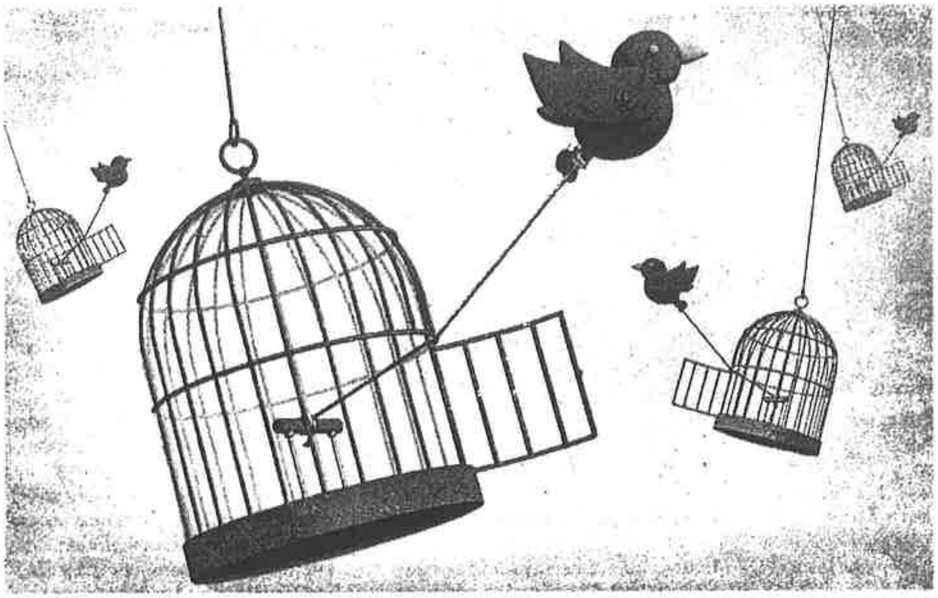
Lubos Pastor, Robert F. Stambaugh, and Lucian A. Taylor, "Scale and Skill in Active Management," NBER working paper, February 2014.

For more papers in this series, or to subscribe, email us at **capideas@ChicagoBooth.edu**.

THE WALL STREET JOURNAL. Monday, November 7, 2016

New Rule Will Help No-Load Funds

But look out: Many 'no loads' are loaded with other fees



BY DAISY MAXEY

MUTUAL-FUND investors may soon see changes on the shelves of fund supermarkets: No-load share classes are likely to dominate the offerings because of a new government conflict-of-interest rule aimed at financial advisers.

The rule, which takes effect in April and requires advisers offering retirement-investment advice to put clients' needs ahead of their own, is expected to reshape the distribution of mutual funds and accelerate the demise of loads, or the fees fund firms charge investors to compensate brokers for selling the funds.

On its face, it is a positive development for investors, who likely will be able to buy funds more cheaply and better understand what they are paying for.

Persistence of 12b-1 fees

But there is still reason for investors to be wary. Many no-load funds will continue to carry marketing or distribution charges known as 12b-1 fees, embedded in the fund's expense ratio. A fund can charge investors a 12b-1 fee of 0.25% annually and still call itself a no-load or no-commission fund.

Among the 19,598 noninstitutional mutual-fund share classes tracked by investment researcher **Morningstar**, 4,218 charge no loads and no 12b-1 fees. (Most are available only in certain 401(k) plans or through financial advisers who charge by assets under management, Morningstar says.) An additional 2,485 share classes have no loads but charge 12b-1 fees of 0.25% a year, or $250 a year for every $100,000 invested.

0.25%

The size of a 12b-1 fee that a no-load fund can impose and still be called 'no load'

"It's messy to have these sales charges wrapped up in the fund's expenses," says John Rekenthaler, vice president of research at Morningstar. Investors would have a clearer idea of what they're paying and to whom if distribution costs were separated completely from investment-management costs, he says.

Some experts say that over time, the Labor Department's new fiduciary rule and an era of greater transparency could begin chipping away at 12b-1 distribution fees just as they have with loads.

Loads have been under pressure for years, leading fund companies in many cases to waive them. The new fiduciary rule is adding to the pressure by encouraging distributors—including fund supermarkets (platforms that permit investors to buy and sell funds from hundreds of companies), major brokerage firms, independent and regional broker-dealers, and bank-and-trust companies—to add no-load-fund share classes to their offerings.

From 2010 through 2015, investors pulled more than $641 billion from load share classes and invested $1.42 trillion in new money in no-load share classes, according to the Investment Company Institute, a mutual-fund trade group. This year through September, investors have pulled an estimated net $113 billion from mutual fund A shares, or those that charge a sales fee up front, Morningstar says.

Many investment managers, meanwhile, are preparing for the possibility of an even more sweeping rule next year. The Securities and Exchange Commission may require brokerage firms and advisers to apply the fiduciary standard across the board to all investors, says Denise Valentine, a senior analyst on wealth management at Aite Group.

To better position themselves, many mutual-fund companies are filing with regulators to create lower-fee or no-load share classes or discussing with their distributors what type of share class they want to offer clients.

Do it the ETF way?

For now, distributors continue to embrace fund share classes with 12b-1 distribution fees.

Broker **Charles Schwab** Corp. stopped selling fund share classes with front-end sales loads in May, but continues to offer an array of funds "with and without a 12b-1" fees, it says. The firm declined to reveal how much of its business comes from share classes with 12b-1 fees.

It would be much clearer for investors, says Mr. Rekenthaler, if the brokerage firm itself charged the distribution fee, and fund companies stopped wrapping it in with their expenses. "That's how it works with an ETF."

Capital Group's American Funds appears headed in that direction.

In late October, the firm filed with regulators to create a new fund share class that will be free of commissions, 12b-1 fees and so-called "sub-transfer-agency fees," which are typically paid to a transfer agent for mundane tasks such as calculating cost basis. The firm hopes to offer the new share class early next year.

"This is our first offering to the individual investor that will have a management-fee structure as opposed to any structure that will go back to compensate for any expense or 12b-1, etc.," says Matthew O'Connor, head of distribution at American Funds.

The new environment is demanding fee transparency and simplicity, he says.

Ms. Maxey is a reporter for The Wall Street Journal in New York. Email her at daisy.maxey@wsj.com.

Turmoil at the top of Pimco rattles US bond and derivatives investors

FT, Sep 30, 2014

MICHAEL MACKENZIE, TRACY ALLOWAY AND TOM BRAITHWAITE – NEW YORK

Upheaval at the top of Pimco rattled US bond and derivatives markets yesterday, as pension funds and other big investors braced for large outflows from the biggest bond manager.

In the first day of trading after Pimco announced its response to the abrupt departure of Bill Gross, its co-founder, some investors decided to get ahead of accelerating outflows by cutting their own exposure to junk-rated and inflation-linked bonds.

The average junk bond yield rose to 6.16 per cent, up from 6 per cent last week, a big move in such a short period. Meanwhile, long-term inflation bonds, signalling inflation expectations for the next 10 years, were pushed below the 2 per cent threshold to hit their lowest level in 15 months.

Over the long haul, US inflation is seen staying above 2 per cent, and a drop below this threshold in the past has reflected a major market dislocation rather than economic fundamentals.

"Bill Gross was the most public advocate for inflation bonds and the market is braced for redemptions and sales," said James Evans, portfolio manager at Brown Brothers Harriman. "We are seeing selling from levered accounts."

Even after 16 months of outflows from its flagship fund, Pimco has massive holdings in bonds ranging from US Treasuries to mortgage securities, inflation-linked assets and corporate debt, including risky junk-rated paper. Overlaying these bond bets are complex derivative strategies in credit and interest rates that Pimco uses to amplify returns or protect portfolios.

The largest US wealth managers, including Merrill Lynch and Morgan Stanley, held conference calls yesterday to discuss their response. "All asset managers are going to have to be careful in how they meet redemptions relative to the challenging liquidity issues in the market," said Larry McDonald, head of US strategy macro group at Newedge SocGen. "You want to ask yourself, does the credit market have the ability to handle large redemptions?"

Scott Mather, one of the managers to succeed Bill Gross running the $222bn Total Return Fund, played down the likely market fallout from the departure of the so-called bond king. The Total Return Fund was "toward the higher end of the quality spectrum", where markets are more deep, he said. "People forget how liquid the bond markets are."

Buttonwood | Gross and net returns

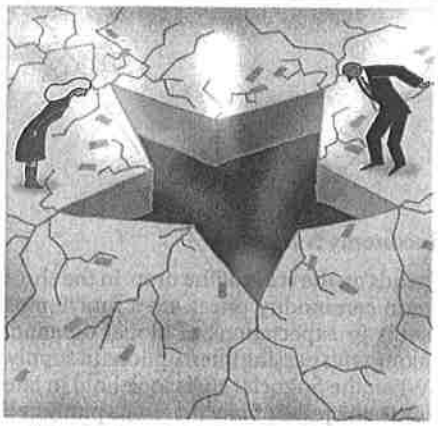
The lessons from a star money manager's exit

THE departure of Bill Gross, the world's best known bond manager, from PIMCO, the investment firm he helped to found, has many potential lessons. At its simplest, it can be portrayed as a Shakespearean drama; the ageing king who refused to loosen his grip on power. Eventually, his subordinates rebelled and overthrew him.

PIMCO's other titan, Mohamed el-Erian, departed earlier this year, prompting a reorganisation of the management team. The next generation of leaders wanted to expand in new areas, something Mr Gross apparently resisted. The Securities and Exchange Commission, an American regulator, recently announced an investigation into pricing at the Total Return fund, the main outlet for Mr Gross's talents, creating the potential for damage to his reputation. Mr Gross ostensibly moved to Janus, a smaller fund manager, to focus more on investment and less on management, but he clearly jumped before he was pushed. The lesson could be that founders are rarely good at succession planning; they often stay in place too long.

A second lesson concerns whether investment firms are wise to rely on the reputation of a "star" fund manager. At its peak, the Total Return fund had assets of $290 billion, a good chunk of PIMCO's $2 trillion total. Mr Gross's occasionally eccentric pronouncements (he once devoted a section of his newsletter to the death of his pet cat) were avidly watched by other investors.

In recent years, he has made some big calls on the bond market. Four years ago, he talked of the British bond market resting on a bed of nitroglycerine; three years ago, he worried that yields would rise when the Federal Reserve ended its second round of quantitative easing. Neither



bearish bet on bonds paid off and the Total Return fund suffered a slump in performance; its return is below the average for similar bond funds over the past five years.

In the short term, PIMCO may be damaged as clients follow Mr Gross to Janus. But the Total Return fund was already suffering outflows because of its faltering performance. In the long run, PIMCO may benefit if clients are drawn more by the strength of its team, and less by the abilities of an individual. Analysing the global bond markets, with their many different countries, currencies, maturities and credit ratings is not a one-man job.

The third lesson is for investors: beware big funds if they are actively managed. If a large bond fund is to beat the market (and justify its fees), the manager probably has to make some big bets on the economy. This is not the same thing as finding a few neglected companies, whose bonds are undervalued because investors have overlooked a crucial fact. Fund managers have no advantage in predicting the economic outlook; indeed, most economists failed to foresee the recession in 2008.

The "big fund" problem previously emerged at Fidelity, where its Magellan equity fund rose to prominence under manager Peter Lynch. After he left in 1990, the fund underperformed the S&P 500 in 12 of the next 20 years, although it did not reach its peak size of $110 billion until 2000. It has since shrunk to $17 billion.

This is a perennial issue. When fund managers perform well, they attract clients and the fund gets bigger. Eventually, however, the fund will stumble. There are three possible reasons for a reversion to the mean. First, the initial strong performance was down to luck, not skill. Second, the initial performance was due to a trend, such as rising technology stocks or falling interest rates (which boost bond prices); eventually, the trend changes. Third, the manager will struggle to excel as the fund grows bigger, perhaps because it has to invest in the shares of bigger companies, or because it must buy more liquid assets; eventually the fund starts to resemble the index.

When performance falters, money will exit again. Thus, in what might be called the Sod's law of fund management, a fund's worst year will probably occur when it is at its biggest. The last clients to jump on the bandwagon will be those who earn the weakest returns.

The same rules do not apply to passive funds, which explicitly try to match the index. In those cases, a bigger fund should lead to economies of scale which can be passed on to clients in lower fees. But the expense ratio of 0.46% on the Total Return fund translates into costs of $1 billion a year at its current size. According to Morningstar, an agency that rates funds, this charge "is a lot more than one might expect given [its] size". Investors are betting big on PIMCO's ability to beat the market.

Economist.com/blogs/buttonwood

Investment funds remain elusive arena for women seeking top posts

FT Nov 29, 2016

CHRIS NEWLANDS AND ALIYA RAM
LONDON

The number of women running investment funds globally has not increased since the financial crisis despite high-profile campaigns to correct female underrepresentation in the asset management market.

Only one in five funds has a female portfolio manager, according to new research examining more than 26,000 funds across 56 countries by data provider Morningstar. That ratio has not improved since 2008.

The problem is particularly acute in the US, Germany, Brazil, India and Poland, where one in 10 funds or fewer have female managers.

Laura Pavlenko Lutton, Morningstar's director of manager research in North America, said: "Our study's findings support the hypothesis that women have had limited leadership opportunities in the fund industry, and, in many well-established areas, we have not observed an improvement since the 2008 financial crisis."

In June a group of Europe's largest asset managers, including Aberdeen Asset Management, Schroders and Allianz Global Investors, joined forces in an attempt to address accusations that the asset management market is an old boys' club that promotes and protects the interests of white, middle-aged men.

Almost 30 companies and industry organisations signed up to the campaign, called the Diversity Project, to try to ensure diverse recruitment across the industry in terms of gender, ethnicity, socio-economic background, age, sexual orientation and disability.

Anne Richards, chief executive of M&G, one of the UK's largest asset management companies, said: "We lost too many women from the industry a few years ago at a critical moment, which has left a big gap. It's not obvious how we're going to fill it."

The Morningstar data showed women are 74 per cent more likely to run a passive fund that tracks an index as opposed to one that tries to beat the market, suggesting the ratio could improve along with a structural shift towards passive management.

FINANCIAL TIMES Monday 12 December 2016

Women run fewer than 5% of alternative funds

PEOPLE

Hedge funds, private equity and real estate funds are less diverse

MADISON MARRIAGE
AND MARY CHILDS

Female portfolio managers run fewer than 5 per cent of the hedge funds, private equity and real estate funds used by most large investors, suggesting the underrepresentation of women in alternative investment is far worse than in mainstream asset management.

One in five mutual funds are run by female portfolio managers, according to figures released last month by Morningstar, the data provider.

The research on women in alternatives — carried out by KPMG, the professional services firm — showed that 80 per cent of industry professionals believe it is harder for women to succeed in the sector than it is for male peers.

Of the 791 fund managers, investors and service providers polled by KPMG, nearly three-quarters of US respondents said it was harder for women to attract capital from investors. Nearly two-thirds of European respondents agreed.

Sandra Horbach, a managing director at Carlyle Group, the US private equity firm, said: "Gender diversity is critical, and we don't have enough of it in the alternatives industry."

Pension funds and other large institutional investors are aware of the problem and seeking to improve matters, according to the report.

One-tenth of investors polled by KPMG said they have introduced special programmes that prioritise investing in funds managed by women, a significant increase from 2013 when only 2 per cent of investors said the same.

Several high-profile pension funds, including the New York City Retirement System and APG, the biggest pension scheme in Europe, recently added questions on gender balance in their due-diligence questionnaires for alternative investment managers.

Eighty per cent of industry professionals believe it is harder for women to succeed in the sector than it is for male peers
Oli Scarff/Getty Images

> 'Gender diversity is critical, and we don't have enough of it in the alternatives industry'

Kelly Williams, who chairs the Private Equity Women Investor Network, said: "Investors are asking the major alternative investment managers why there are not more women on their teams. As a result, [companies] are increasing their focus on recruiting diverse candidates."

Patricia Lizarraga, managing partner at Hypatia Capital Group, a private equity firm that focuses on investing in companies run by women, added: "I think [the situation for women] is improving. There is a cultural shift.

"The world is clamouring for balanced leadership, and therefore women in the space are finding themselves empowered to talk about a subject that for many, many years was taboo. That is changing the dynamic of how women in finance feel about themselves and it is positive."

The findings come 10 months after the publication of research by Rajesh Aggarwal and Nicole Boyson, academics at Northeastern University in Boston, which showed that female hedge fund managers have more difficulty in raising capital than men, despite performing better than male counterparts.

Nearly two-thirds of the investors polled by KPMG said the biggest barrier to investing in funds run by women was the lack of supply or talent.

Laurie Weir, investment director at Calpers, the largest US public pension scheme, suggested that large investors were not working hard enough to find talented female managers.

Number of portfolio manager positions held by women falls for six years straight

Female fund managers in decline

CHRIS NEWLANDS

The number of female portfolio managers running money in the US has fallen every year for the past six years despite continued efforts to try and bring more women into frontline asset management.

According to figures from Morningstar, the data provider, the ratio of male to female fund managers has widened each year since 2009, prompting condemnation from diversity campaigners who believe investors are ultimately being harmed by the huge gender gap between male and female managers.

Helena Morrissey, chief executive of BNY Mellon subsidiary Newton and a leading activist for gender equality in the workplace, said: "This bothers me because I truly believe portfolio management is a great choice of career for women. Fund companies and their clients are losing out [as a result of the falling number of female fund managers]. But I am not shocked or surprised."

The data, given to news service 929 Media, found that female portfolio managers now account for less than 7 per cent of the 7,293 money managers running US mutual funds, down from just over 10 per cent in 2009.

Chad Astmann, a partner at Heidrick & Struggles, the headhunters, and head of its asset management practice in North America, said: "It is hard for me to understand exactly why [this is the case]. It is a really surprising statistic, as a lot of the focus of our clients in asset management has been on increasing the number of women in portfolio management."

Critics believe the imbalance is a significant issue for fund companies, subjecting them to biases in their decision making. Evidence suggests this can open them up to repeated investment mistakes.

Mr Astmann said: "It is almost indisputable that having diversity of thought within any business — particularly when you are [trading securities] or putting together a portfolio — is critical to ensuring you are aware of any biases."

At the end of 2014, FTfm asked the 10 largest independent fund houses in the US and Europe to provide information on how many women they employ and at what level.

Only one fund company shared that information: Aberdeen Asset Management. The remaining nine groups declined, including BlackRock, Vanguard, Fidelity Investments, Franklin Templeton and Capital Group in the US, and Schroders, Union Investment, Lombard Odier and Pictet Asset Management in Europe.

Anne Richards, chief investment officer of Aberdeen, said: "There is no quick fix. But it is quite anachronistic that the fund rating agencies still focus on a single named individual on a fund while many funds are managed by a team. Rating teams by their diversity and including that as part of the overall 'star' rating might increase the focus on diversity."

She added: "There are sound business reasons for correcting this. Mixed teams make better-reasoned decisions and more easily avoid groupthink."

Reasons given for why the number of female portfolio managers has fallen include the assertion that women have been put off more by the tarnished image of the financial services market than men.

Ms Richards said: "On average, women appear to place more importance on feeling that their job has a clear value to society.

"I believe fund management has such value, but that has obviously been a tougher sell in recent years."

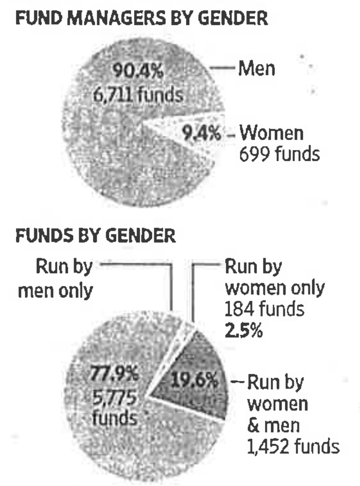
Ms Morrissey added: "Fund management is a great career for anyone who wants to be judged on results, not hours at a specific desk. Therefore it is great for women and men who want their career to be part of, not the only, thing in life. I could not have had nine children and reached a similar career point if, say, I had been a corporate finance lawyer."

The imbalance is not confined to the US. Figures released last year by Tilney Bestinvest, the brokers, found that only 7 per cent of UK retail investment funds are managed or co-managed by female fund managers.

Additional reporting by Christopher Smith, a reporter at 929 Media

You've Got Males

Gender breakdown of 7,410 portfolio managers of U.S. mutual funds



Note: As of March 31, U.S. mutual funds only. Some percentages don't add to 100% due to rounding.
Source: Morningstar
THE WALL STREET JOURNAL. 7/7/2015

Rival Vanguard wants voluntary tests without the involvement of regulators

BlackRock backs tough stress tests

FT Oct 3, 2016

CHRIS FLOOD

BlackRock has come out in favour of proposals by global regulators to introduce more stringent stress tests on mutual funds, pitting the world's largest asset manager against its rivals, who are opposed to the plans.

A number of asset managers have already begun voluntary stress testing of their funds to ensure they can meet redemptions during times of market upheaval, and many are unhappy about being forced to collect and send this data to regulators due to the costs involved.

The Financial Stability Board, the Basel-based organisation that monitors the global financial system, proposed regular stress testing of individual funds in June in a bid to ensure asset managers have sufficient means to meet withdrawal requests from investors.

BlackRock said in its written response to the FSB: "We believe there is merit in developing principles for the stress testing of individual open-ended funds. Liquidity risk stress testing is one tool that can be helpful to ensure fund managers are maintaining appropriate liquidity."

However, Vanguard, the world's second-largest fund house, said asset managers should be left to carry out their own stress tests without the involvement of regulators.

"We would not support policy recommendations that direct managers to use specific tools. Prescribing tools encourages herding in fund portfolios and trading, which could amplify market stress," the Pennsylvania-based fund company said.

"We do not agree that authorities should require stress tests and provide guidance on how they should be conducted."

Vanguard's stance is supported by the Securities Industry and Financial Markets Association, the New York-based trade body that represents hundreds of asset managers, banks and securities companies.

Sifma said it would be "premature" for authorities to consider stress testing mutual funds. "There is a conceptual problem with the very notion of stress testing the capital adequacy of a mutual fund, where the objectives, methods, and costs and benefits are wholly undefined and therefore immeasurable," the organisation said.

The US Securities and Exchange Commission, which is also in the process of finalising rules aimed at improving levels of liquidity, said last year that there were big discrepancies in the approach asset managers take in monitoring their ability to respond to large withdrawals.

"Some funds employ liquidity risk management practices that are substantially less rigorous," the US regulator said.

Concerns about liquidity have been fuelled by Third Avenue's decision in 2015 to block withdrawals from its high-yield bond fund. The New York-based manager halted redemptions even though the bond fund had $200m in cash, representing more than 20 per cent of assets.

The suspension of withdrawals by seven commercial property funds following the UK's vote to leave the EU in June has added pressure on regulators to act.

Joel Shapiro, associate professor of finance at the University of Oxford's Saïd Business School, said the introduction of mandatory stress testing would help "improve confidence" in the industry. But he added that the proposals were likely to meet widespread opposition from asset managers.

"Stress tests are enormous data-collecting exercises for those involved. This is probably an expense that fund managers will not relish, given the rising costs in the industry," he said.

The FSB has also suggested that consideration should be given to broader "system-wide" stress testing that would attempt to assess what would happen if there were simultaneous withdrawals from a large number of funds.

BlackRock and Vanguard are united in their opposition to this proposal. BlackRock noted that insurers, pensions, foundations, endowments, sovereign wealth funds and family offices are not required to report their activities to the FSB. Consequently any move to implement system-wide stress tests would be pointless, according to the New York-based company.

"System-wide stress testing, macro stress testing of all mutual funds, or stress testing of all funds managed by an asset manager, would be predicated upon faulty assumptions, insufficient data and a misunderstanding of fund structures and asset-owner behaviour.

"We caution that aggregated stress tests of this nature are at best meaningless and at worst could result in misguided policy actions that risk creating the problems that the FSB and other regulators are seeking to avoid," it said.

THE WALL STREET JOURNAL. Wednesday, October 12, 2016

Mutual Funds Win Key Concessions

BY DAVE MICHAELS

WASHINGTON—Mutual funds soon will face new regulations to reduce the risks of an investor exodus during a panic, though they have managed to win some concessions that will make the rules more flexible.

The Securities and Exchange Commission is set to release the new rules Thursday, a key part of its plan to modernize supervision of the $15.7 trillion sector. The once staid business of pooling stocks and bonds has become more complex and risky, as funds adopt strategies that involve harder to sell securities, derivatives and leverage.

Economists at the International Monetary Fund and the Federal Reserve Bank of New York have warned that mutual funds are vulnerable to destabilizing runs similar to those that can afflict banks if investors demand their money back faster than funds can sell the underlying assets.

The SEC's new rules are aimed at reducing that risk. Many investment managers object in principle, saying mutual-fund shareholders are predominantly long-term investors who keep their money in funds even during severe market downturns. The new rules, they say, could unnecessarily hurt their investing strategies and returns.

A new draft that SEC staff circulated to commissioners in recent weeks reflects the industry's complaints, people familiar with the matter said.

The SEC's original proposal, released a year ago, would require funds to maintain a reserve of liquid assets that could be turned into cash within three days. In theory, those easy-to-sell assets would act like a shock absorber, giving funds a cash lifeline during desperate times. The bar would be higher for funds holding less-liquid assets such as emerging-market bonds or bank loans than it would have been for plain vanilla stock and bond funds, the rule proposal said.

Regulators have never before imposed such a requirement. Funds argued in comment letters that it was too onerous.

Critics including Federated Investors Inc. wouldn't be able to add higher-yielding securities if those purchases caused their share of very liquid assets to tick below the required minimum, complicating how they managed their investments.

The SEC's final rule keeps the three-day minimum as a goal, but give funds more flexibility to comply, the people said. In essence, as long as funds have policies designed to meet the standard, they would be given short-term wiggle room when the requirement conflicts with their normal investing strategies.

The SEC's original proposal also required funds to estimate how many days it would take to sell off each of their holdings, a complicated task for funds that own dozens and sometimes hundreds of securities or derivatives contracts.

Vanguard Group and Federated Investors wrote in comment letters to the SEC that no portfolio manager could know precisely how long it would take to sell every stock or bond they own, because the ease of trading varies in different market conditions.

"Federated believes that the components of the proposed rule requiring the categorization of individual security positions are onerous, illogical, and may, if executed, be misleading to shareholders," the company wrote earlier this year.

The SEC's final rule will scale back the requirement, the people said. Funds instead would be allowed to estimate the liquidity of a group of similar assets, such as investment-grade bonds or emerging-market stocks, although they would be responsible for studying specific holdings that could be exceptions to the norm.

Adi Sunderam, an associate professor at Harvard Business School, challenged the industry's complaints about the rule. "How can you claim this is pretty liquid if you have no idea how long it would take to sell it?" he said. "The answer that 'we don't know' does not give me a lot of confidence."

Industry groups say mutual funds regularly assess their ability to sell enough of their portfolio to meet redemptions on any given day.

In addition, many funds have access to lines of credit and other funding sources that can generate cash quickly.

An SEC spokeswoman declined to comment on any changes to the proposal, citing the agency's practice of staying silent on the details of rules that haven't been finalized.

The draft still could change amid internal agency negotiations before SEC commissioners vote on the final version Thursday.

The SEC's effort grew out of broader regulatory concerns that asset managers perform many of the same functions as big banks but face lighter regulation.


STEPHEN VOSS FOR THE WALL STREET JOURNAL

The SEC is set to release new rules Thursday for mutual funds.