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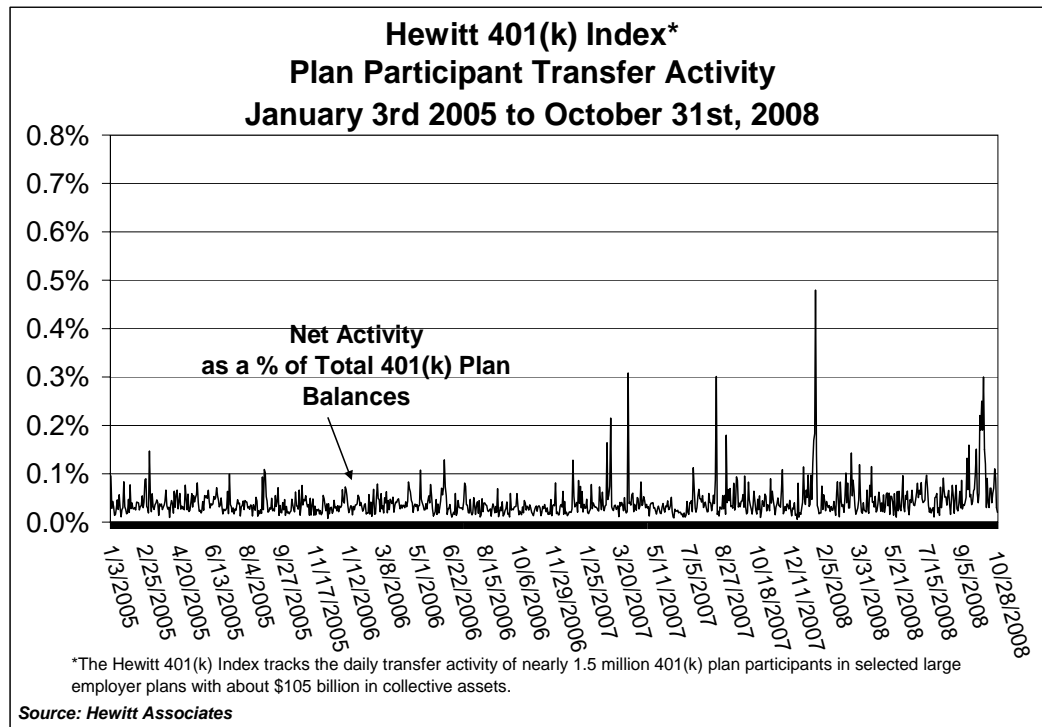
Mutual Fund Flows and Portfolio Managers' Activity: The Calm after the Storm

Stock Fund Redemptions in Recent Weeks Were Modest and Reassuring

NEW YORK, NY – November 6, 2008 – After peaking during the second week of October, investor redemptions from stock mutual funds subsided to nearly normal levels, according to Strategic Insight, a business intelligence provider to the mutual fund industry.

Although October redemption activity was elevated, high-volume defensive switches were concentrated in just a few days of extreme stock market anxiety, mostly during the second week of the month. And even during such high-volatility days, stock fund redemptions reached just 0.3% of stock fund assets: this means that \$997 out of every \$1,000 stayed put. This is not surprising, because research from Strategic Insight (and similarly from the Investment Company Institute) consistently shows that during the past 30 years, **spikes in fund redemption activity tend to be short-lived and non-recurring**. For all of October, stock fund net redemptions are estimated at roughly 1.5% of equity fund assets in aggregate — not surprisingly, at the high end of historical experiences, according to preliminary estimates by Strategic Insight.

These observations were confirmed in a number of SI interviews. They are also exemplified by the *Hewitt Associates 401(k) Index* ([available here](#)), which captures the daily activity of nearly 1.5 million investors in 401(k) plans. The data illustrated below shows that among these investors, transfers from equity funds to safer alternatives, while rising periodically, remained minimal in the past two weeks following the early October spike. The Hewitt data shows the portion of balances transferred on any one day during the days of highest anxiety in early October was just three out of every \$1,000 invested (equal to 0.3% of assets). Clearly, 401(k) investors are picking asset-allocation strategies and sticking with them.



Why have industrywide stock fund flows been relatively stable during a period of such market volatility? **US Equity funds are anchored by retirement accounts.** More than 60% of US equity fund assets are in retirement accounts, including 401(k) accounts, IRAs and variable annuities. These represent more stable assets, as investors have absorbed 25 years of education on dollar-cost averaging and regular contributions. And most of stock fund assets intended to be used only many years from now, investors face no need to withdraw cash during times when value of their holdings are declining.

Stock Funds: Portfolio Managers Sold Fewer Stocks than Investor Redemptions Imply; in September Stock Fund PMs Actually Added Liquidity to the Stock Market

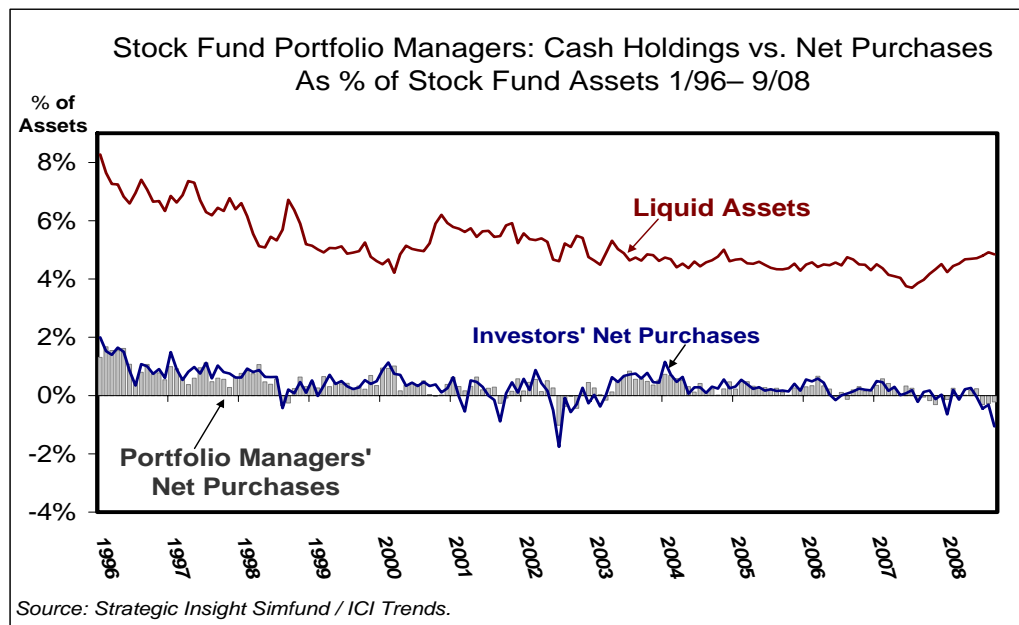
- **Equity funds' portfolio managers continue to act as buffer during times of extreme net redemptions by shareholders:** In September 2008, equity fund portfolio managers' net redemptions of stocks was just **\$13 billion**, according to the ICI, or roughly 0.2% of all such fund assets. That amount was just **one-fifth of net redemptions by investors (which exceeded \$60 billion)**, or roughly 1% of assets in stock funds). Also: during September, net investments in equity ETFs, which are not captured in the ICI data above, reached \$49 billion.
- **Taking together modest net liquidations of stocks (\$13 billion) and net purchases of stocks by ETFs (\$49 billion) shows that the mutual fund industry was a net**

liquidity provider to the stock market during September (despite a 10% price correction) to the tune of \$36 billion.

- Equity funds' portfolio managers routinely keep some assets in cash and use this cash to buy when stock prices seem attractive. As in previous periods, these stock fund managers, sitting on roughly \$300 billion in cash, "buffered" September's net redemptions and most likely some of the selling pressures in October's net redemptions by fund shareholders, and net sold a smaller volume of individual stocks. (In addition, it's worth noting that given the net purchases by equity-driven ETFs, aggregate liquidity pressures due to mutual fund portfolio net sales were quite small.)

Stock Fund Portfolio Managers Have Significant Cash Holdings to Meet Investor Redemptions Even During Periods of High Redemption Activity

As the chart below make clear, a steady availability of cash and other liquid resources in stock funds allows fund managers to offset investors' net redemption activity. Thus, the structure of the mutual fund business enables portfolio managers to act as buffers; portfolio managers' purchasing patterns lag investors' buying activity, and portfolio manager redemptions also lag and mitigate short-term emotionally-driven redemptions by investors.

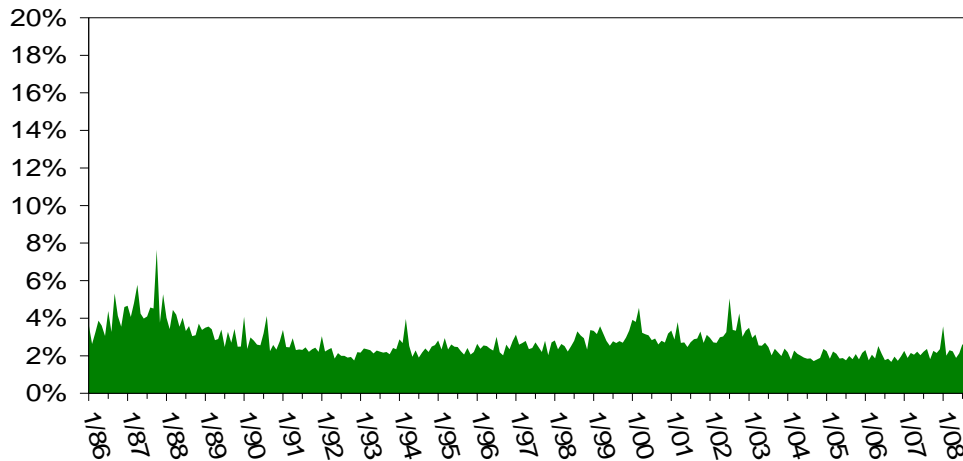


Looking Ahead: What to Expect?

During times of financial uncertainty, investors reduce, rather than increase, the turnover of their financial assets. Intuitive belief that accelerating redemptions will occur in a sustained manner during a bear market contradicts the empirical evidence. Redemption

activity tends to decline during a bear market, with the exception of brief and modest spikes during sharp down-market weeks. Why? Investors' psychological aversion to realizing losses partly explains such bear-market behaviors. Fund shareholders are more likely to react to market downturns with paralysis than with massive shifts in allocations.

Monthly Equity Fund Outflow Rates 1986 - October 2008



Source: Strategic Insight Simfund MF / ICI Trends. SI estimates 10/08.

Overall, the major factor affecting equity mutual fund flows during an extended period of market uncertainty is not overwhelming redemptions but a decrease in new purchases. Yet, steady retirement-related investing (including the recurring demand for lifecycle funds-of-funds, which was boosted by the 2006 Pension Protection Act), dollar-cost-averaging deposits, the ongoing shift to managed funds from individual stock dependency both outside and inside retirement plans, and some opportunistic buying at lower prices will combine to prevent equity fund net redemptions from becoming sustained and large.

“Although events of the past few months have shaken peoples’ confidence, mutual fund shareholders have stood firm overall,” commented Avi Nachmany, Strategic Insight’s Director of Research. “Despite rare spikes in defensive switches, mutual fund shareholders have largely kept their ‘buy-and-hold’ attitudes lately.”

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*In its 22nd year, Strategic Insight is a respected research firm for the mutual fund and wealth management industry, providing clients with in-depth studies, consultation, and electronic decision support systems. **Strategic Insight assists over 250 organizations worldwide, including the largest mutual fund management companies operating in the U.S. and the largest insurance companies serving the VA business. SI clients are responsible for about 90% of all U.S. mutual fund assets.** For more information, visit our home at www.sionline.com.*