

February 6, 1998

# Monthly Mutual Fund Report

## Statistics for December 1997 Year - End Report

---

### Sales and Redemptions

Total assets for all funds increased \$58.7 billion, or 1.3 percent, to \$4.5 trillion in December. Net new cash flow into the industry, a measure of the demand for mutual fund shares, was \$20.9 billion. The market value of the industry's assets increased by \$37.8 billion.

Total assets of equity funds increased \$39.3 billion, or 1.7 percent, to \$2.4 trillion. Net new cash flows into equity funds were \$16.8 billion in December, compared with \$18.2 billion in November.

Total assets for bond and income funds increased \$16.4 billion, or 1.6 percent, to \$1.0 trillion, with a net new cash inflow of \$5.6 billion in December and an increase in the market value of holdings of \$10.6 billion.

Assets of taxable and tax-exempt money market funds rose \$3.0 billion, an increase of 0.2 percent and 0.7 percent, respectively.

In 1997, total industry assets increased \$950.6 billion, or 26.9 percent, of this increase \$377.9 billion was due to net cash flows. The increase in total assets for equity funds during 1997 was \$648.9 billion, or 37.1 percent compared to 37.8 percent in 1996. Of this growth, \$231.3 billion, or 13.2 percent, was due to net new cash flows, while in 1996, 17.5 percent was due to cash flow. Bond and income funds' total assets increased \$144.6 billion, or 16.3 percent, in 1997 with a net cash flow of 5.0 percent, compared to 11.0 percent increase in assets in 1996. Total assets of money funds increased \$157.1 billion in 1997, or 17.4 percent.

### Liquidity Ratios

Liquidity Ratios for equity and bond funds, at 5.2 and 4.9 percent respectively, remain below their historical averages of 8.8 percent and 7.1 percent (figure 4). Equity funds are at their historic low and bond funds are close to their low of 4.5 percent. These low liquidity ratios can be attributed to several factors. In 1995 settlement periods for stock and bond transactions were reduced from the 5 business days to 3 business days, this meant that less liquidity was required to secure redemptions until cash was received from the sale of securities. Recent revisions to



the tax code, the elimination of the short-short law, allow investment companies to derive a greater portion of their income from assets held less than 90 days, this has enabled mutual funds to increase their options activity. A futures sale is a cash transaction and provides funds with immediate access to their assets without incurring the opportunity cost of holding cash. Banks have also been increasing their committed lines of credit to mutual funds, while simultaneously lowering their fees. Therefore, the cost of these lines of credit are now lower than alternative forms of liquidity. With increasing size, funds are able to maintain the same level of security with lower levels of liquidity as the variation in their net sales per dollar of assets declines, other things equal.

### **Asset Composition**

As international and global stock market indexes fell, the share of assets held in international and global funds continued to decline (figure 5) and has reached its lowest level since late 1993.

### **Weekly Flows**

During January, the net cash flows into funds rose and fell commensurately with changing returns on assets (figure 6). During the last week in January, equity funds, including aggressive growth, small caps, and international funds, had positive returns just under 5 percent and net cash inflows between 0.5 and 2 percent.

Asia-Pacific funds experienced very volatile cash flows and returns in January, ending the month with cash inflows of almost 20 percent of assets. Japanese funds have maintained steady cash inflows for the past three weeks, while their returns have declined, becoming negative during the last week in January.

### **Capital Market Returns and Volatility**

The S&P 500 ended 1997 at 970.43 with a total return for the year of 33.3 percent. So far in 1998, the index ended January at 980.28 with an annualized return of 14.4 percent. The volatility for the daily returns on the S&P 500 has increased to 18.6 percent, its highest value during the most recent business cycle (figure 8). Volatility and returns for the Salomon Brothers' bond index remain high but stable.

For more information please contact Kathryn Cosgrove (617) 973-3198

Figure 1  
**Sales of Mutual Funds**

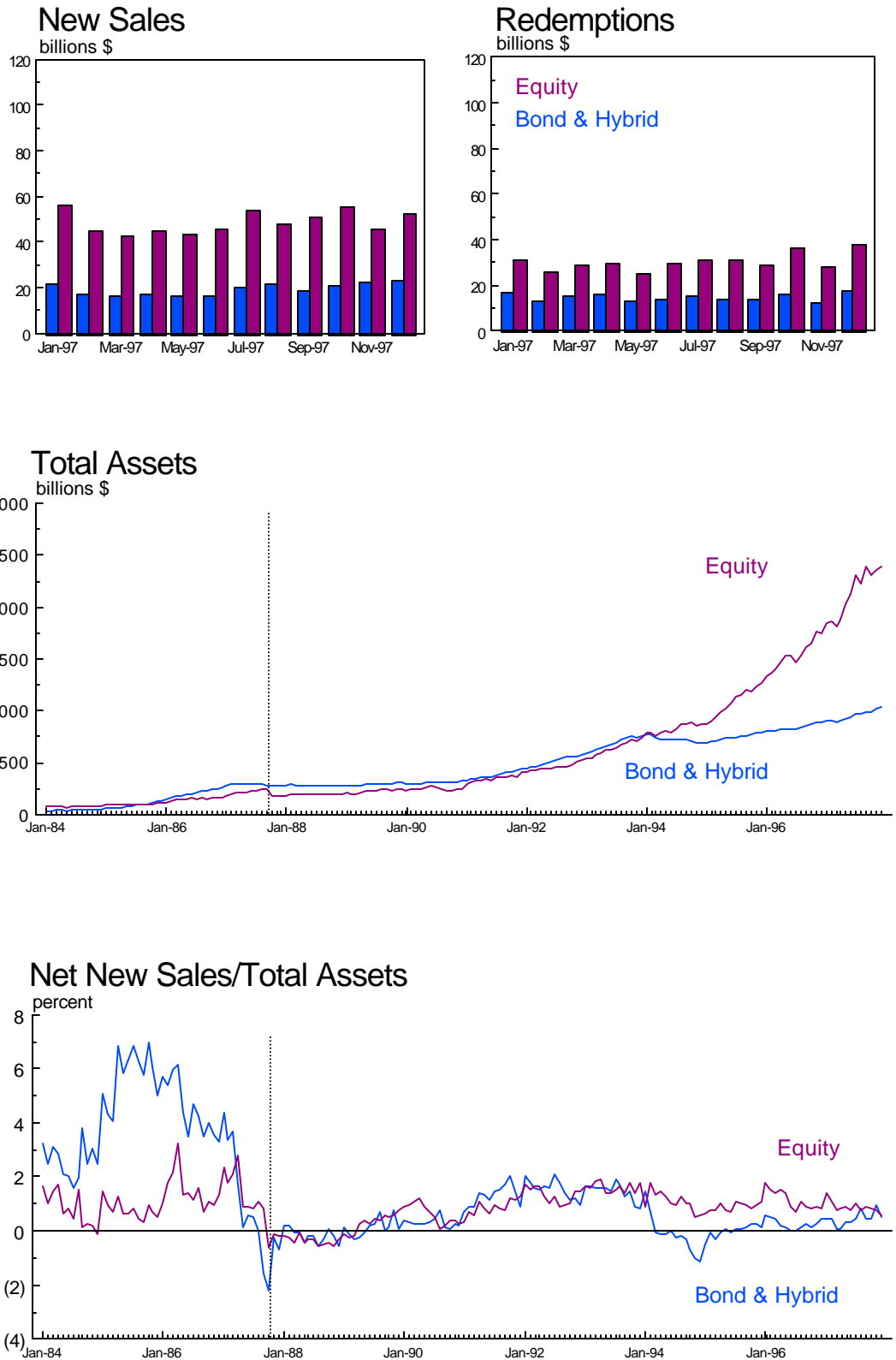


Figure 2

# Composition of Mutual Funds' Financial Assets

(percent of Total Financial Assets)

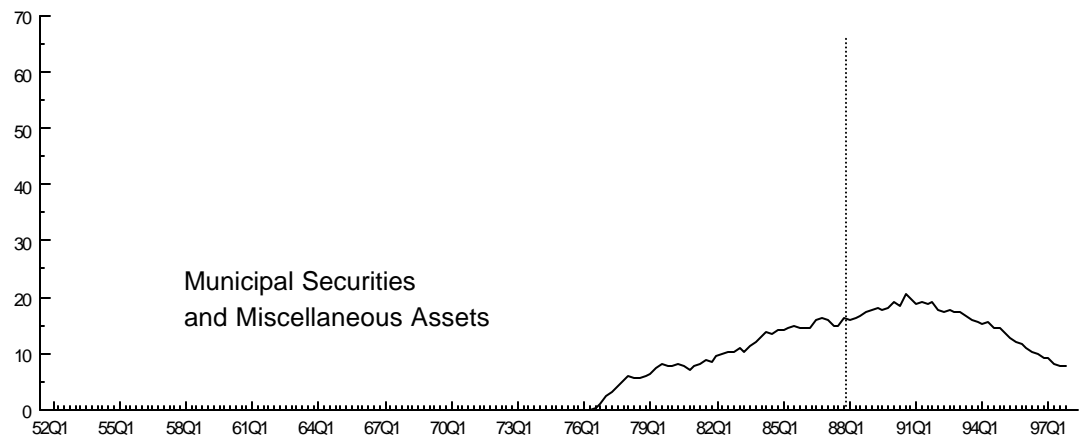
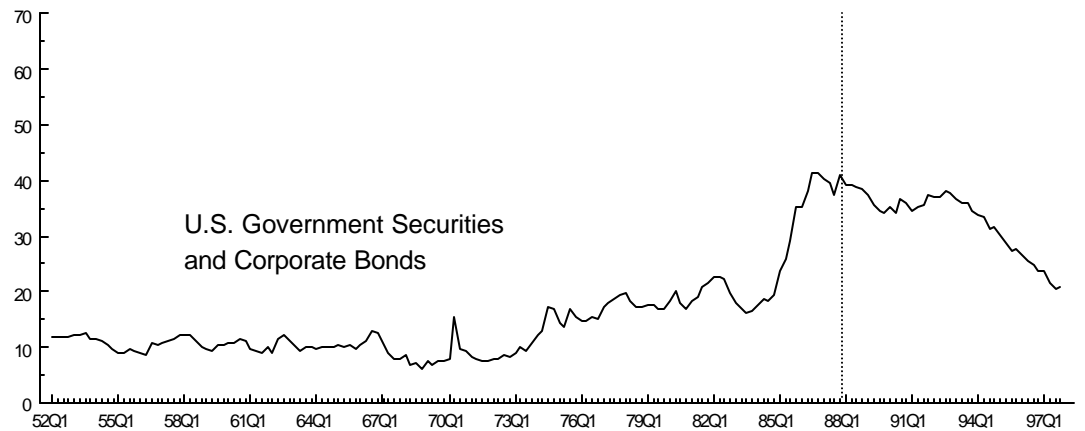
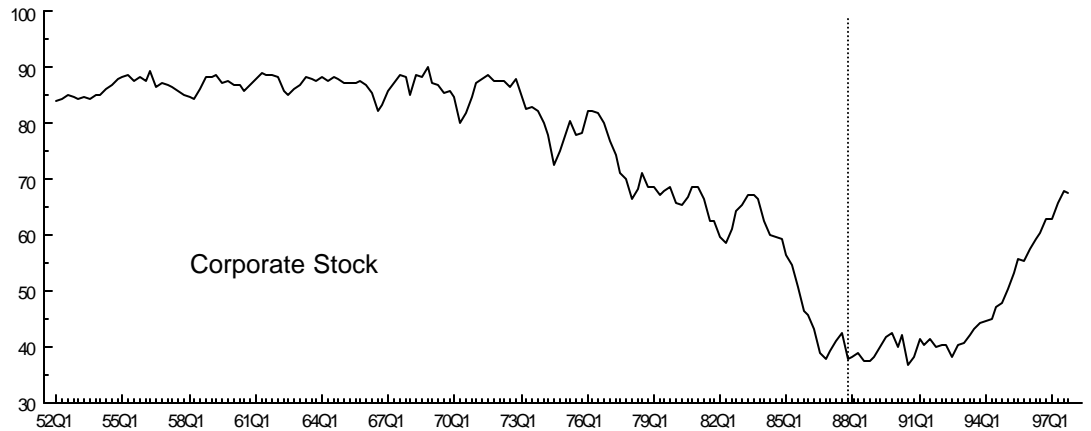


Figure 3  
**Net Portfolio Purchases**  
 (percent of Total Assets)

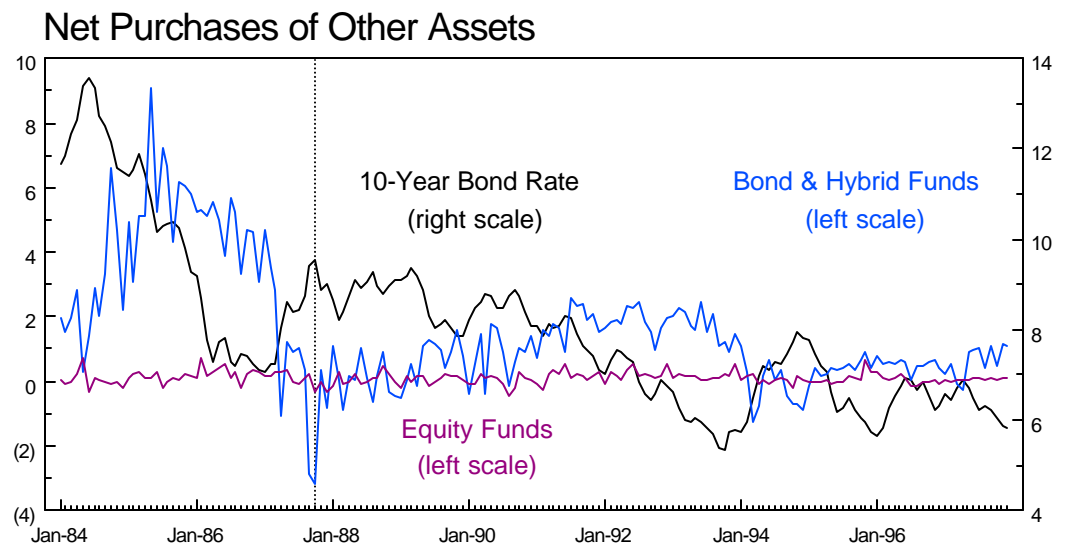
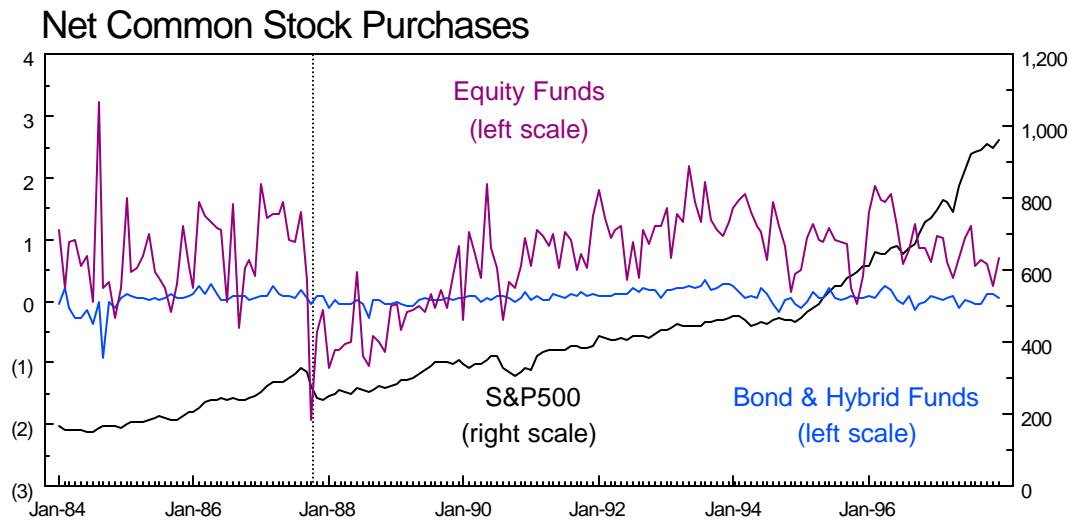
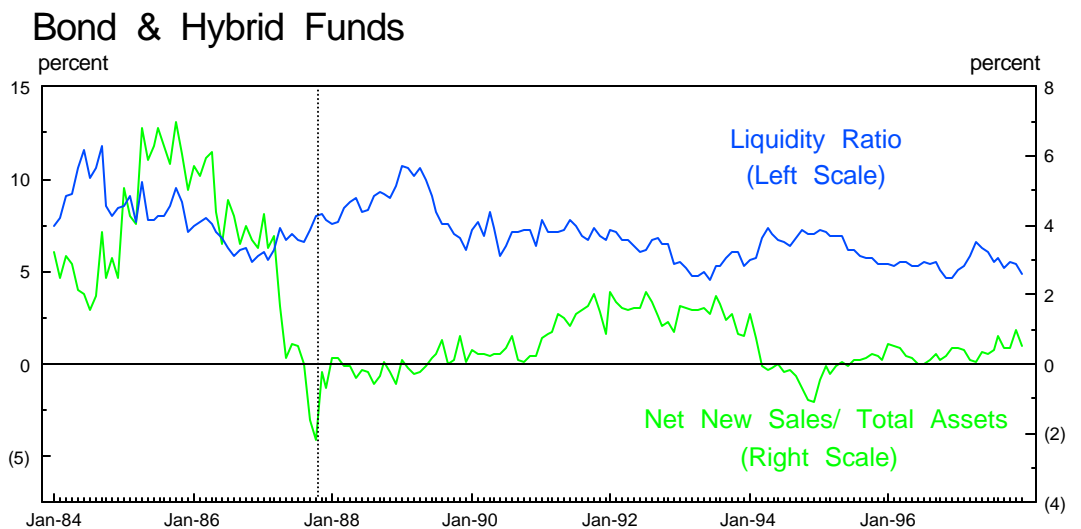
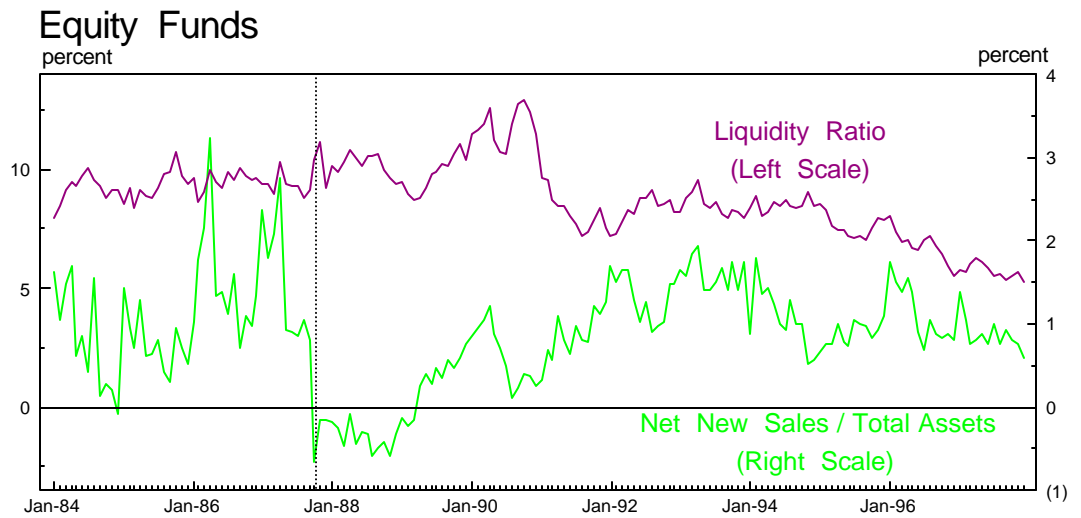
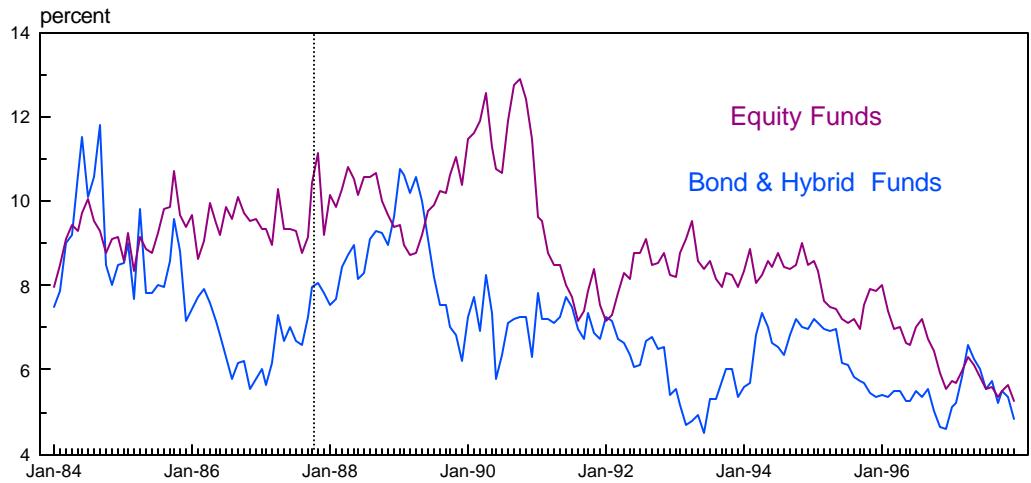


Figure 4  
**Liquidity Ratio\***



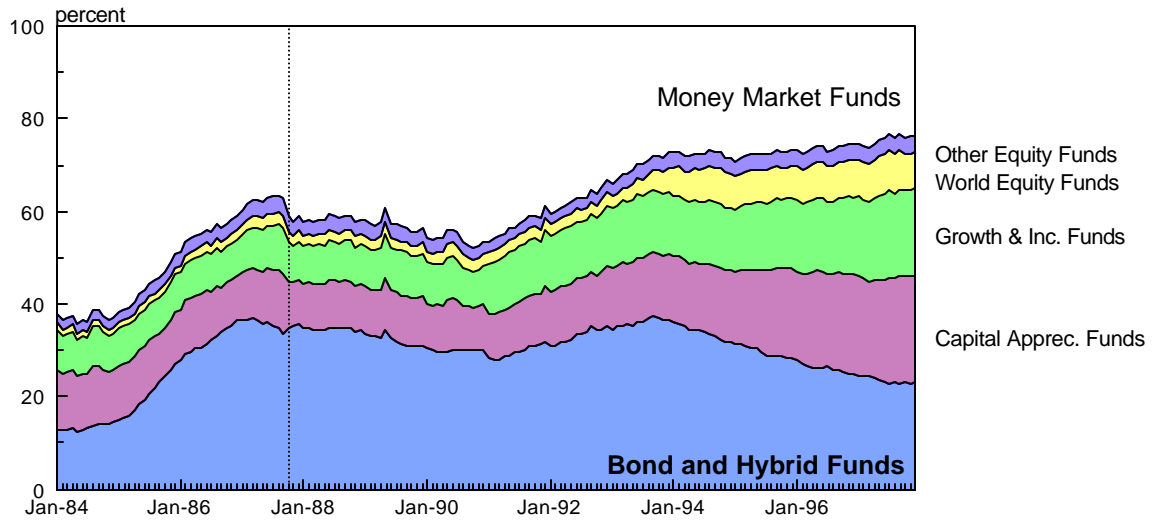
Source: Investment Company Institute

\*The Liquidity Ratio is the Percent of Total Assets held in Cash and Short-Term Securities.

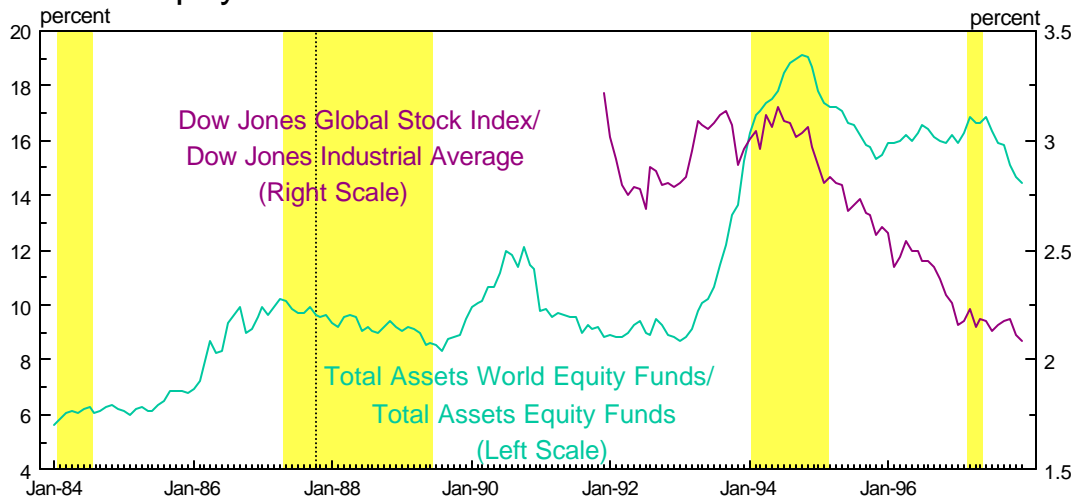
Figure 5

# Industry Composition

(Shaded Regions Indicate Periods of Rising Fed Funds Rate)



## World Equity Funds



## Capital Appreciation Funds

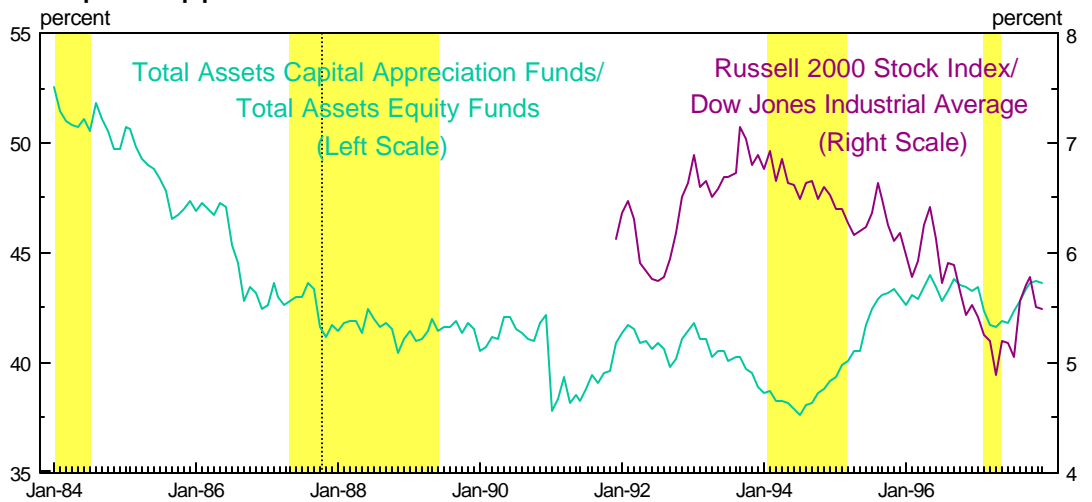
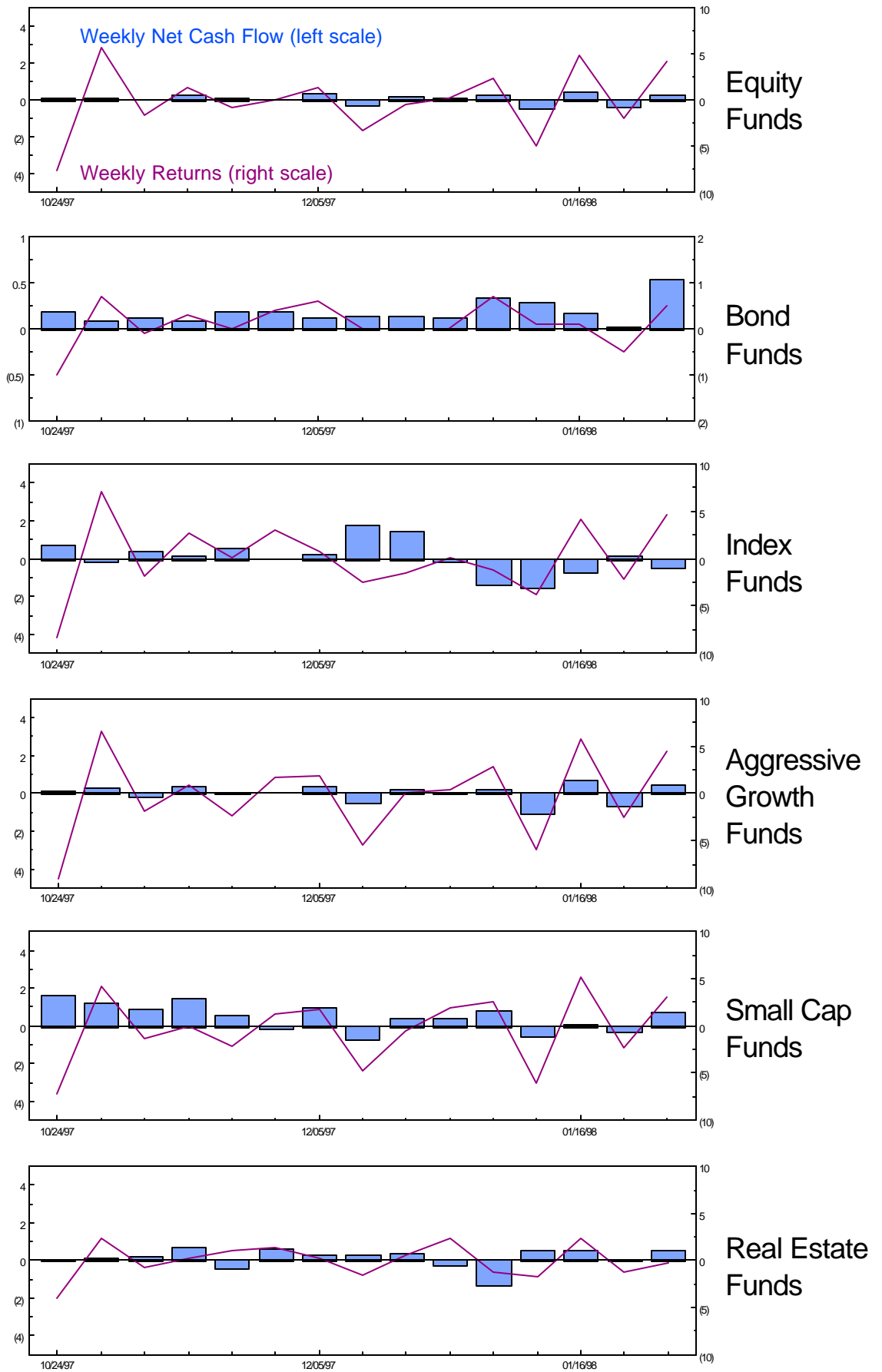


Figure 6a

# Weekly Flows into Mutual Funds

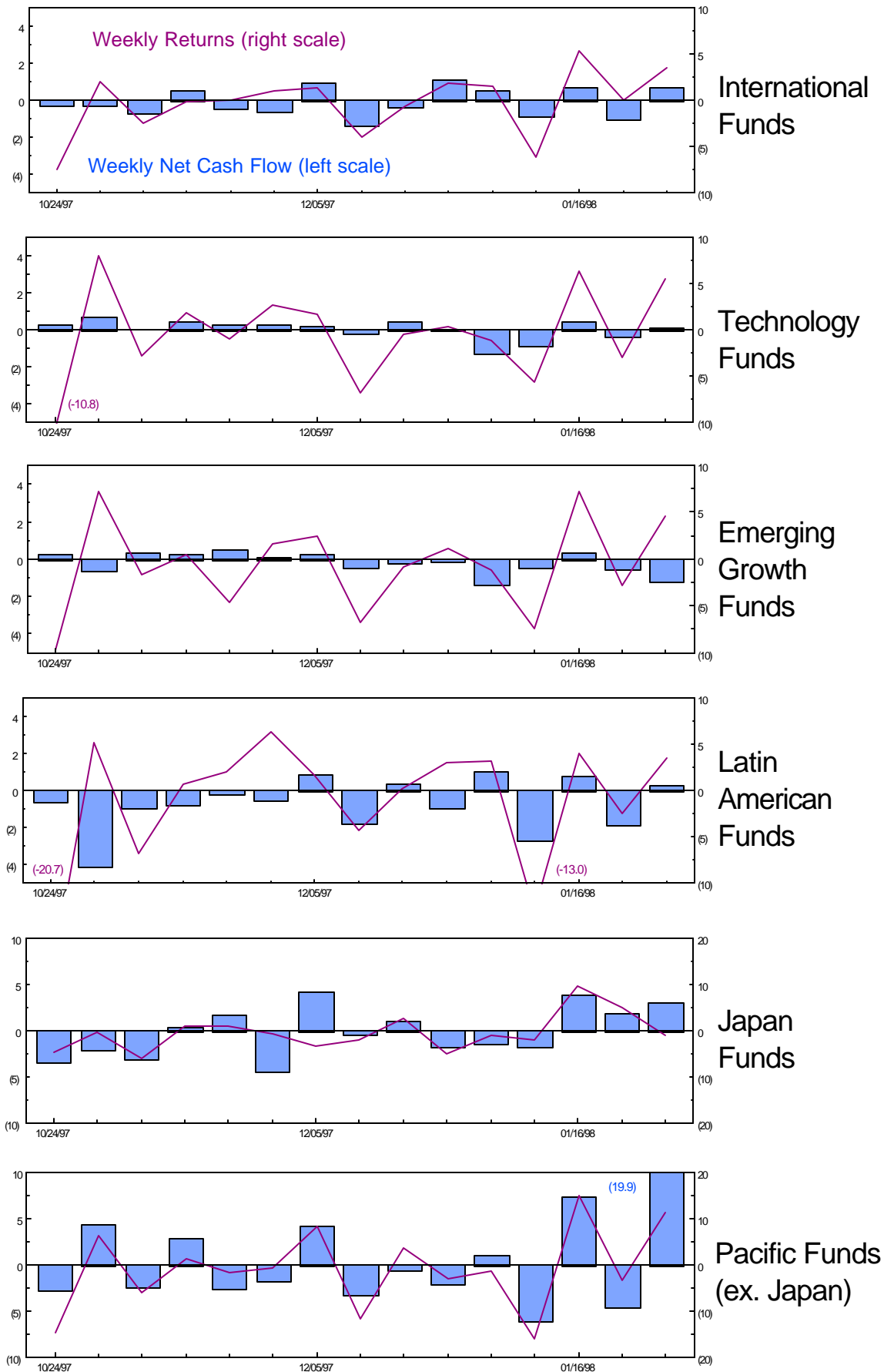
(percent of Total Assets)



Source: Mutual Fund Trim Tabs



Figure 6b  
**Weekly Flows into Mutual Funds**  
 (percent of Total Assets)



Source: Mutual Fund Trim Tabs

# Figure 7 Net New Sales By Investment Objective

(Shaded Regions Indicate Periods of Rising Fed Funds Rate)

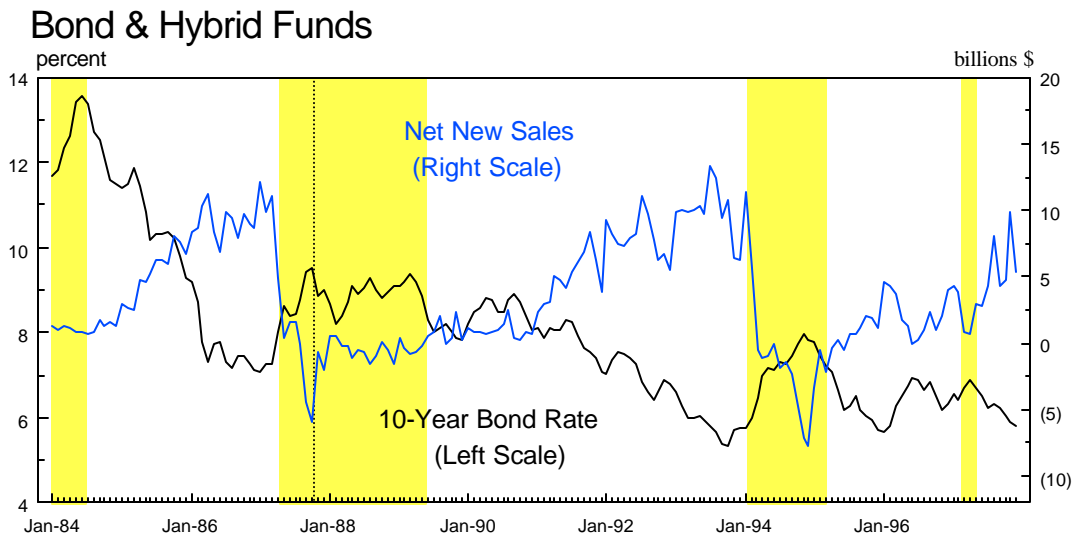
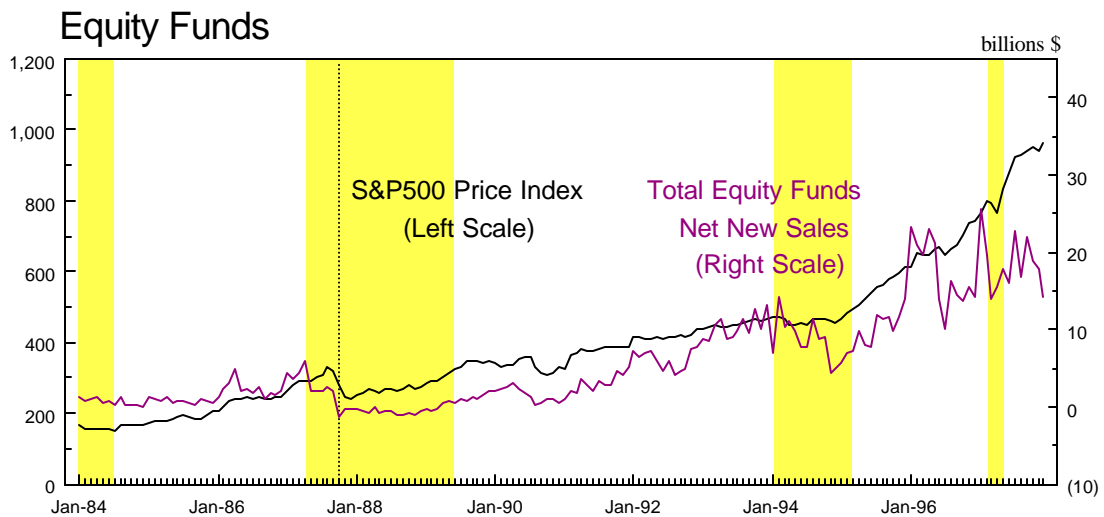


Figure 8  
**Capital Market Returns and Volatility**

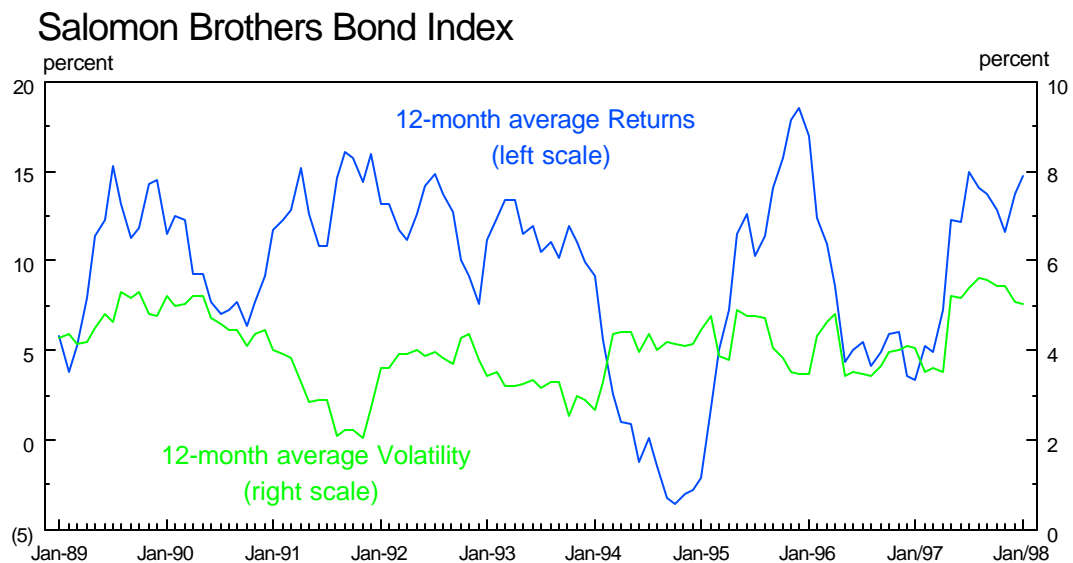
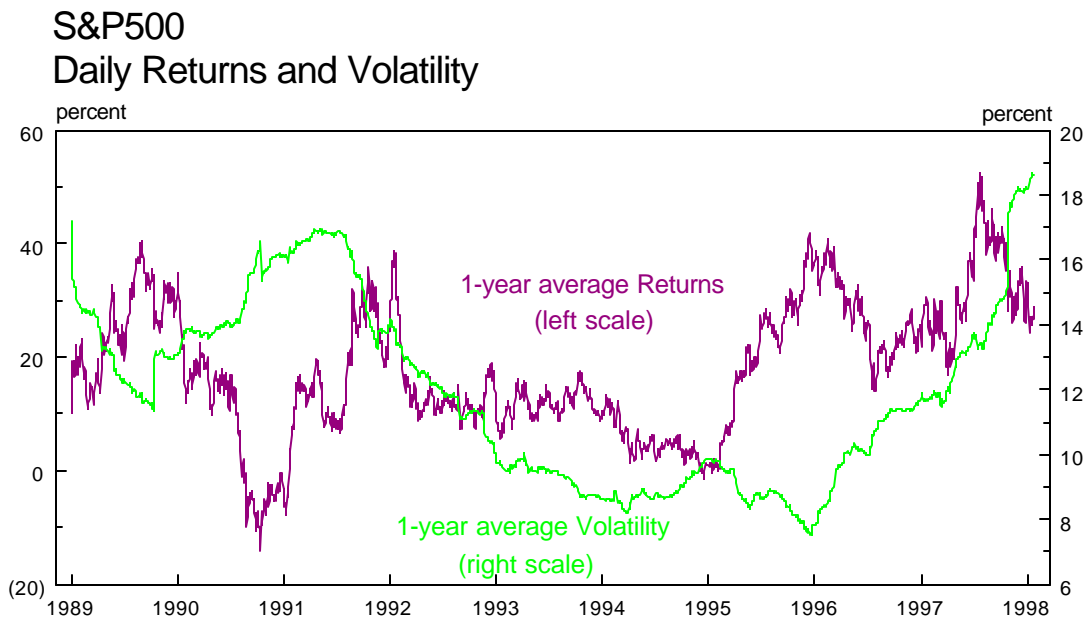
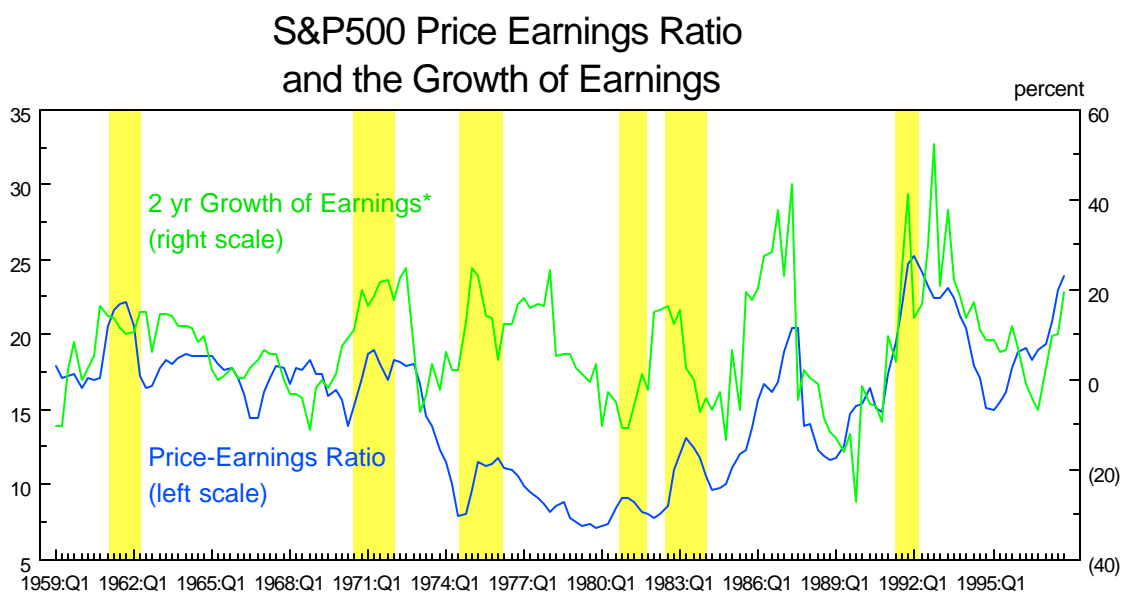
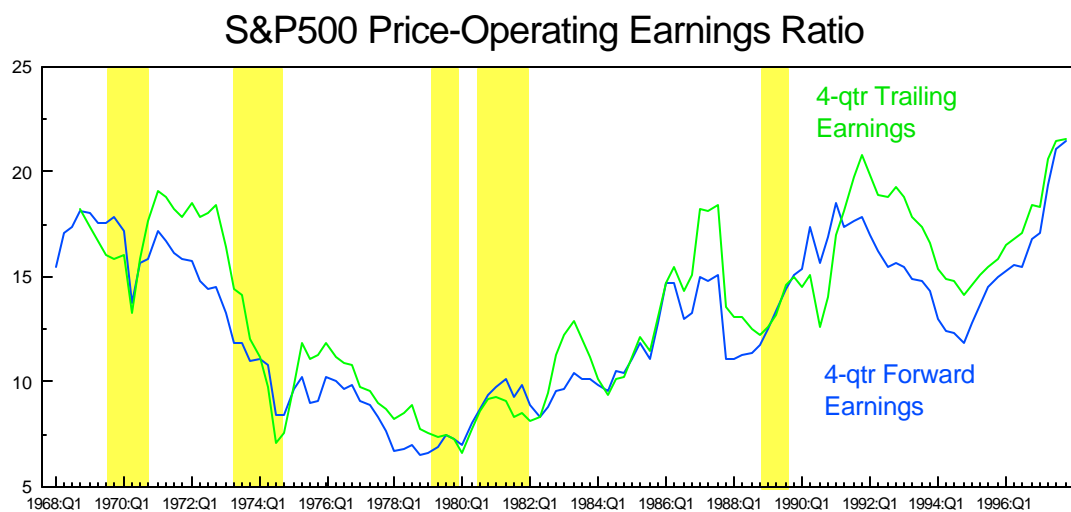
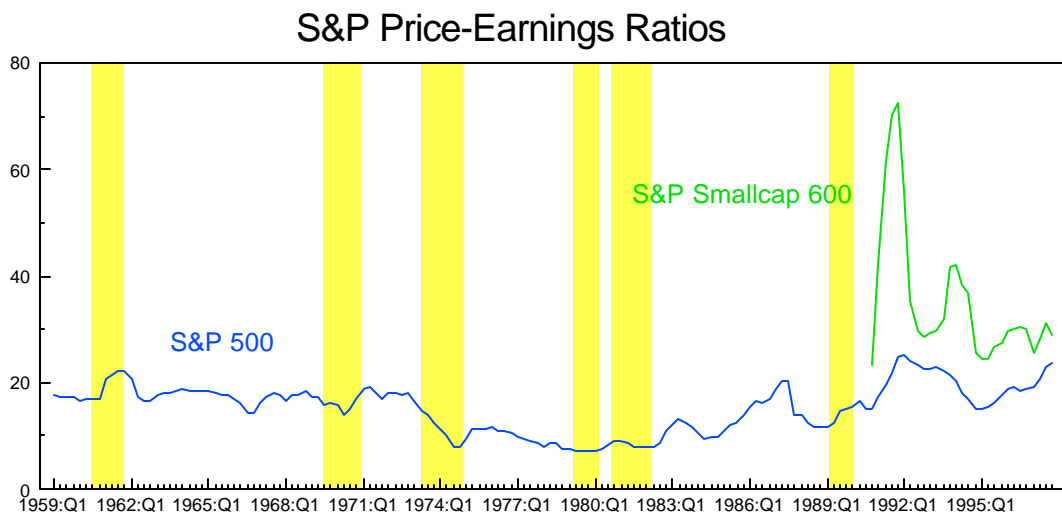


Figure 9



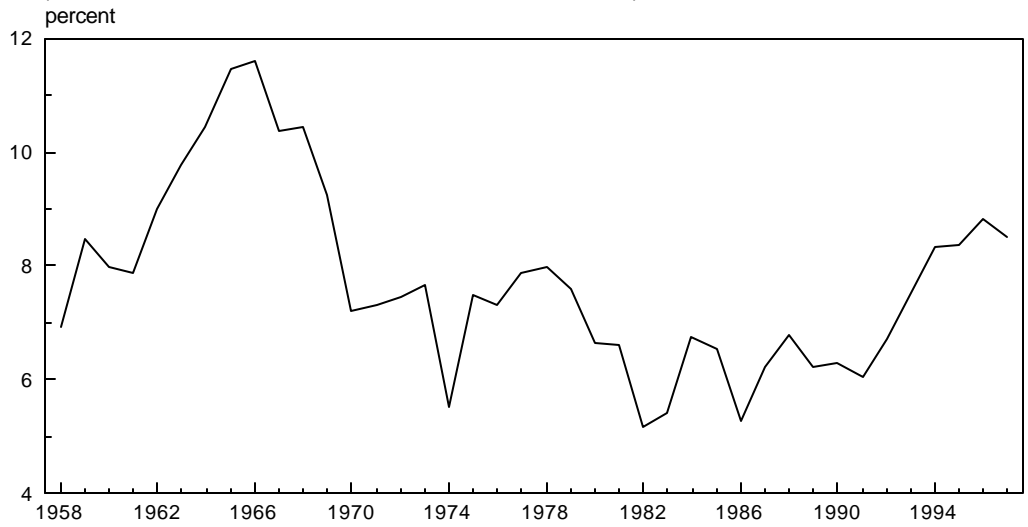
\* Growth of earnings over subsequent 8 quarters. Current observations use forecast of earnings from macro projections.

source: First Call, DRI, Bloomberg

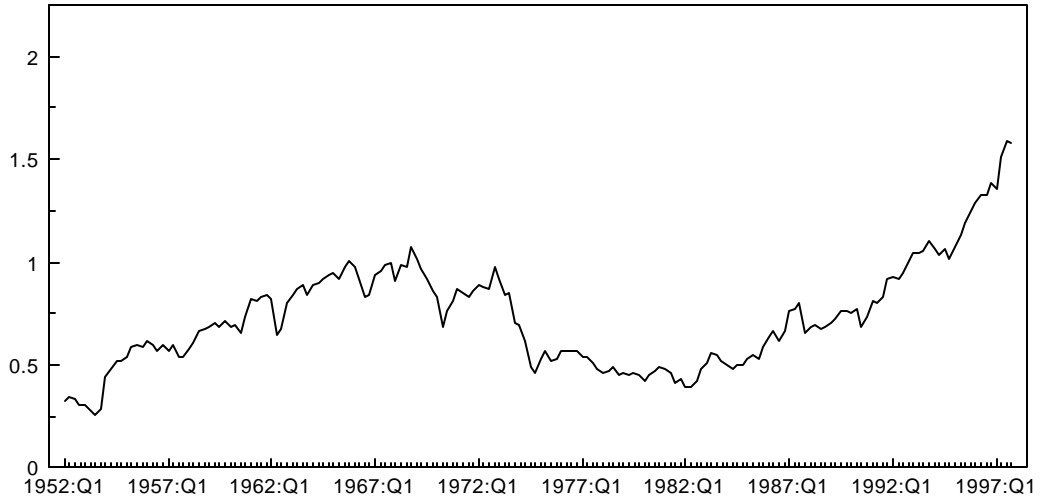
Figure 10

### Real Rate of Return on Nonfinancial Corporate Equity

(from National Income and Flow of Funds Accounts)

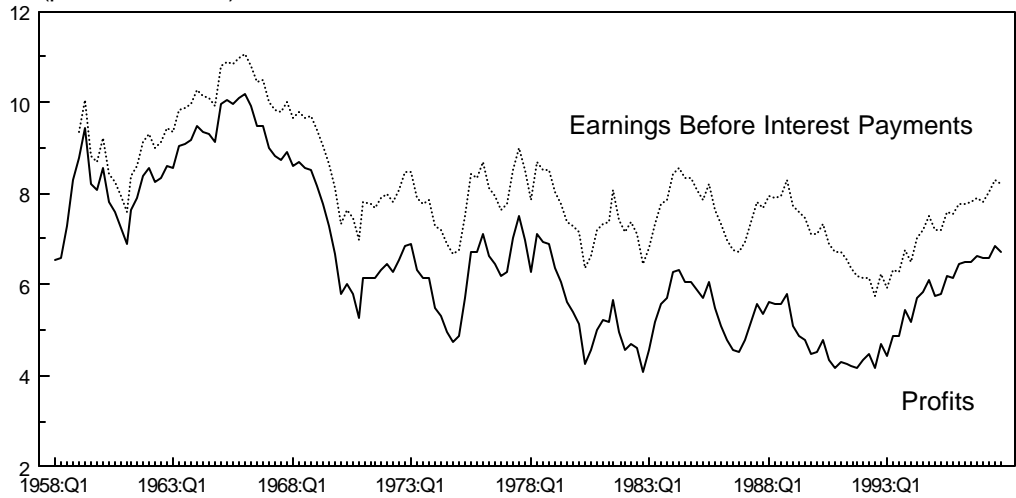


### Tobin's Q\*



### Profits of Nonfinancial Corporations

(percent of GDP)



\* Market Value of Equity plus Net Interest Bearing Debt/ Current value of Land, Inventories, Equipment, and Structures