Investors fond of bonds so far in 2019

By Editorial Staff *Thu, Feb 28, 2019*

'Retail investors remain skeptical of the ferocious stock market rally early this year,' said David Santschi, director of liquidity research for TrimTabs. 'While bond mutual funds are drawing big inflows, all equity mutual funds have lost an estimated $14.9 billion in February.'

After experiencing a record outflow in December 2018, bond funds have rebounded in 2019. Taxable and municipal bond funds alone had net inflows of $39 billion in January, according to Morningstar. Of that amount, passive taxable bond funds received a record $27.6 billion in the first month of 2019.

The tilt to fixed income continued in February. Bond mutual funds received an estimated $28.1 billion through February 26. The category was on track for its second-largest monthly inflow in five years, according to a release from TrimTabs Investment Research.

"Retail investors remain skeptical of the ferocious stock market rally early this year," said David Santschi, director of liquidity research for TrimTabs, which is based in Los Angeles. "While bond mutual funds are drawing big inflows, all equity mutual funds have lost an estimated $14.9 billion in February."

U.S. equity funds and sector equity funds had a combined outflow of $12.1 billion in January, in a month when all long-term funds had net inflows of $39.1 billion. Almost equal amounts flowed in and out of active U.S. equity funds during January. Passive U.S. equity funds had an outflow of $3.8 billion.

January was the first time since March 2018 that open-end funds enjoyed stronger inflows than ETFs. The $34.1 billion advantage in flows was the greatest since March 2014. Over the 12 months ending January 31, open-end funds had $184 billion in outflows versus ETFs' $240 billion in inflows. Active long-term funds lost $325 billion while passive long-term funds gained $391 billion.

Because of January's strong equity returns, managed portfolios, such as target-date funds, with fixed allocations to individual funds may have been forced to trim their U.S. equity funds, Morningstar analysts Kevin McDevitt and Michael Schramm commented.

On the one hand, two S&P500 funds—Fidelity's and Vanguard's—were among the ten biggest gainers in the month. But two S&P500 ETFs—SPDR S&P500 and iShares Core

S&P500—were among the ten biggest losers of flow in January.

One consistent story-line has been investors' endless pilgrimage to Vanguard funds. You could attribute that to Vanguard's low costs and passive investing, but those can be found elsewhere. Vanguard's brand strength, which reflects trust, may be the driving factor there.

Highlights from Morningstar's fund flow report for January included:

- Overall, long-term flows recovered in January, with $39.0 billion in inflows after $83.0 billion of volatility-induced flight in December. Previous years saw much higher January inflows, however, with $132.0 billion in 2018 (following the passage of tax cuts) and $63.0 billion in 2017 (following the presidential election). Over the past 12 months, long-term flows have remained weak with only about $56 billion in net inflows.
- Taxable bond funds, as a Morningstar Category, netted $31.5 billion in January 2019, the group's best performance since January 2018. Passive taxable-bond funds, as mentioned above, received a record $27.6 billion.
- Ultra-short bond funds received only $2.3 billion, their weakest month since September 2017. "Investor enthusiasm for ultrashort bond funds waned significantly," wrote McDevitt and Schramm. "This may have owed to the Fed's announcement that further rate increases are on hold."
- Diversified emerging-markets funds led Morningstar Categories in January with $10.9 billion in inflows, the category's best month since January 2018.
- International equity funds bounced back with $14.2 billion of inflows in January after a reciprocal amount of outflows in December, most likely driven by tax-loss selling.
- Among the largest U.S. fund families, Vanguard dominated with $19.7 billion in inflows. Specifically, Vanguard Total Bond Market II Index saw $6.9 billion inflows this month, January's greatest inflows for a vehicle.
- The mild surprise from U.S. fund families in January was the weak performance of iShares, which collected just $400 million, the firm's worst showing since June 2018.

Morningstar estimates net flow for mutual funds by computing the change in assets not explained by the performance of the fund, and net flow for U.S. ETFs shares outstanding and reported net assets.