June was a ‘risk-off’ month for equities: Morningstar

By Editorial Staff *Thu, Jul 26, 2018*

‘With the global population aging and many investors focused on capital preservation, equity demand among fundholders remains tepid,’ said the Morningstar Direct Asset Flow report for June.

U.S. equity funds saw net redemptions of $20.8 billion in June 2018, as long-term U.S. open-end mutual funds and ETFs saw their greatest outflows since August 2015, according to the Morningstar Direct Asset Flows Commentary for June.

June ended the third-worst first half for U.S. equity flows in a decade, after 2015 and 2009. Sector-equity, international-equity, allocation, alternative, and commodity funds all had net outflows. In their largest monthly outflow in at least a decade, large-blend funds alone saw net outflows of $19.4 billion.

Only taxable-bond and municipal-bond funds had inflows. Taxable-bond funds were the only long-term group with big inflows, adding $15.5 billion in June. Relatively conservative ultrashort-bond funds attracted almost $5.5 billion, and intermediate government funds gained about $3.1 billion in inflows. High-yield bond funds surrendered $3.4 billion in outflows.

Over the past 12 months, ultrashort-bond funds received $50.5 billion for a 38.2% organic growth rate. Since the start of Federal Reserve rate-hikes in December 2015, ultrashort-bond funds have attracted $85.3 billion, up from just $14.0 billion in the previous two and a half years.

For equities, it was a different story. “In a bit of a paradox, the greatest net outflows came from active U.S. equity funds, which had $17.1 billion in net redemptions versus negative $3.7 billion for passive funds,” the Morningstar analyst wrote.

Among individual funds, index offerings fared especially badly. Five funds–SPDR S&P 500 ETF SPY, iShares Core S&P 500 ETF IVV, Vanguard Institutional Index VINIX, Invesco QQQ Trust QQQ, and Vanguard Total Stock Market Index VTSMX–saw combined outflows of $14.7 billion.

While a few large passive funds had substantial outflows, the majority (about 70%) had inflows. About 26% of actively managed U.S. equity funds had modest inflows; T. Rowe Price Small-Cap Value PRSVX added about $660 million.

“Because ETFs are often used as trading vehicles, it’s hard to know how much of last month’s U.S. equity passive outflows reflect a change in investor sentiment versus simple trading or rebalancing. Looking from a broader perspective, U.S. equity inflows haven’t been terribly strong over the past decade,” the Morningstar report said.

“Since July 2008, U.S. equity funds have collected about $254 billion in inflows. That’s a big number, but it’s not that impressive when you consider that’s starting from a base of $3 trillion,” the analyst wrote.

“Yes, the past 10-year period includes a chunk of the credit crisis in 2008-09, but it also includes a historically long bull market. With the global population aging and many investors focused on capital preservation, equity demand among fundholders remains tepid.”

International equity funds saw outflows for the first time since September 2016, estimated at $9.8 billion. The average diversified emerging-markets equity fund was down 8.9% over the past three months. Net redemptions of about $8 billion from diversified emerging-markets equity funds represented the greatest net outflow in at least a decade.

Investors pulled a combined $625 million from emerging-markets bond and emerging-markets local-currency bond funds. Vanguard Total International Stock Index enjoyed about $7.3 billion in inflows, but emerging markets represent only about 17% of its assets. Foreign large-blend funds had $4.3 billion in inflows while Vanguard Total International Stock Index VGTSX, a core holding, collected $7.3 billion.