Metrics of the 2013 bull market

By Kerry Pechter *Thu, Jan 16, 2014*

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What a year it was for U.S. equity investors. And to think that a huge crash made it possible.

The average U.S. stock fund gained 31% in 2013, nearly double the 15.9% earned by international stock funds, according to Strategic Insight. A strong finish to equity markets in 2013 elevated stock funds/ETFs net flows to over $400 billion for the year as a whole. Bond funds, following four years of dramatic inflows in aggregate exceeding $1 trillion, reversed course beginning in the spring as interest rates started to rise. Flows to bond funds were negative each month since June 2013, and such redemptions reached nearly $50 billion in the fourth quarter.

"2014 should witness the continuation of stock investors' re-engagement," said Avi Nachmany, Strategic Insight's research director, in a release. "Demand will remain across a wide spread of U.S. and international stock investment approaches, but will also include bond funds anchoring asset allocation programs and especially those positioned for an improving global economy."

Mutual funds

Equity funds netted $253 billion in 2013 (excluding ETFs and VA funds), led by strategies for globally diversified developed markets. While bond funds in aggregate suffered modest net redemptions for the year, flexible 'alt' bond funds and those positioned for a rising interest rate environment, such as floating rate, short maturity, and global, continued to experienced positive flows.

Exchange-traded products

U.S. equity ETPs (ETFs and other exchange-traded products) netted $19 billion during December and $188 billion in 2013. "Notably, U.S. equity ETFs outsold International ETFs last year by a ratio of over 2:1, whereas international funds were the top-sellers among mutual funds. Overall, however, trends in net sales of ETPs mirrored their mutual fund counterparts, with equity fund gains contrasting a pullback from bond funds," said Alan Hess, a Strategic Insight analyst.

Capital gain distributions

The rising stock markets since 2009 that have caused leading stock indices to eclipse prior records in 2013 triggered dramatic increases in capital gain distributions last year. Such distributions are estimated to exceed $300 billion for the year, more than tripling 2012 distributions, and were the second highest in history (following 2007 $414 billion according to the ICI). Among stock funds paying capital gains in December 2013, the average ratio was 7.3% of NAV for U.S. equity funds and 5.9% for international equity funds.

For those who own actively managed stock funds in taxable accounts (not in IRAs, 401(k)s, or VAs), representing about one-quarter of stock fund assets, the tax impact of such high capital gains distribution would trigger a greater interest in the tax advantages of index funds and ETFs. “One area of intriguing promise is actively managed ETFs, a segment of intense innovation activity for the coming years,” added Nachmany.

Flows by distribution channels

Mutual fund flows during 2013 were highest via the Independent/Regional BD channel, which accounted for 33% of fund flows via intermediaries. Such BDs also contributed an estimated 18% of ETF flows last year. ETF distribution was led by RIAs, who controlled 23% of ETF flows in 2013 (more than double their 9% share of mutual fund flows). Interestingly, ETF flows via banks (which can include significant institutional investor influence) accounted for 17% of total ETF flows – more than four times such banks’ small and falling share of mutual fund flows (4%).

“Fund managers are increasingly focusing their distribution efforts in more targeted ways across the intermediary-sold market. This includes evaluating opportunities based on differences in fund and ETF acceptance, asset velocity and pace of redemptions, adoptions of innovative funds, and more. As the industry continues to mature, such focus continues to increase in importance,” said Dennis Bowden, Strategic Insight’s Assistant Director of Research.