

Morningstar DirectSM Asset Flows Commentary: United States

Morningstar Research

May 2018

Data through April 30, 2018
U.S. Mutual Funds and Exchange-
Traded Products

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Executive Summary

- ▶ Passive U.S. equity funds resumed their dominance over their active counterparts, collecting \$18.2 billion in inflows while active funds lost about \$11.4 billion to outflows.
- ▶ International equity funds remained more popular than their domestic brethren, pulling in about \$11.1 billion, with strong demand for foreign large-blend and diversified emerging-markets funds.
- ▶ Taxable-bond funds fared even better, bringing in \$25.3 billion and led by ultrashort and intermediate-term bond funds.
- ▶ Vanguard was near the top of the fund-family league tables with \$12.3 billion in inflows, but BlackRock's iShares eclipsed that figure with about \$17 billion. Vanguard's growth continues to slow year over year.

Passive Equity Funds Return to Form, While Bond Funds Defy Expectations

April 2018 asset flows returned to form after the prior month's anomalies. Following two consecutive months of outflows, U.S. equity funds rebounded with estimated inflows of \$6.8 billion. That rebound owed to passive U.S. equity funds resuming their dominance over their active counterparts, collecting \$18.2 billion in inflows while active funds lost about \$11.4 billion to outflows. Overall, trailing 12-month U.S. equity flows remain negative—to the tune of \$42.6 billion, or a 0.6% decline.

Exhibit 1 U.S. Equity Category Group Monthly Flows

U.S. Category Group	Total Estimated Net Flows \$Mil		
	Apr 2018	1 Year	Assets \$Bil
U.S. Equity	6,557	(42,479)	7,879
Sector Equity	(9,098)	13,610	890
International Equity	11,125	263,869	3,348
Allocation	(2,913)	(25,436)	1,338
Taxable Bond	25,254	351,496	3,740
Municipal Bond	(1,610)	30,546	693
Alternative	(1,154)	10,279	221
Commodities	2,431	7,463	105
All Long Term	30,591	609,348	18,215
Money Market	(9,029)	124,754	2,766

Source: Morningstar Direct Asset Flows.

Core large-blend funds were once again the most-popular Morningstar Category by far, with \$10.8 billion in inflows. To put this dominance in perspective, large-blend funds took in \$14.4 billion for the year to date through April. The second most-popular U.S. equity category was mid-cap blend funds, which collected about \$200 million over the same period. The most-popular fund year-to-date is Vanguard Total Stock Market Index VTSMX with \$19 billion in inflows, followed by Vanguard 500 Index's VFINX \$15.1 billion.

International equity funds remained more popular than their domestic brethren, pulling in about \$11.1 billion. However, amidst a volatile start to 2018, inflows did decline for the third consecutive month. Still, international equity funds enjoy the highest year-to-date organic growth rate, 2.72%, among the major asset categories. Commodity funds have the highest year-to-date growth, at 7.44% on \$7.1 billion in inflows.

Core foreign large-blend funds took in the lion's share of \$5.6 billion, but diversified emerging-markets demand remained strong, with \$4.5 billion in inflows. That's surprising given that emerging-markets equity funds have fallen 6.5% on average over the past three months, due in part to greater volatility and a strong U.S. dollar.

Exhibit 2 Top- and Bottom-Flowing Morningstar Categories

Estimated Net Flows \$Mil	April Flows			1 Year Total	Assets \$Bil
	Active	Passive	Total		
Top					
US Fund Large Blend	(2,585)	13,388	10,803	14,383	71,780
US Fund Foreign Large Blend	90	5,620	5,710	73,156	142,263
US Fund Ultrashort Bond	1,336	4,277	5,613	124,344	47,244
US Fund Intermediate-Term Bond	448	4,503	4,951	5,170	149,642
US Fund Diversified Emerging Mkt:	1,545	2,966	4,511	26,072	59,224

Estimated Net Flows \$Mil	April Flows			1 Year Total	Assets \$Bil
	Active	Passive	Total		
Bottom					
US Fund Large Value	(4,769)	1,329	(3,440)	(53,184)	(41,168)
US Fund Muni National Short	(2,022)	297	(1,725)	232	(43,135)
US Fund Large Growth	(1,104)	(518)	(1,622)	(55,251)	(10,684)
US Fund Technology	(1,444)	1	(1,443)	1,178	861
US Fund Health	(658)	(763)	(1,421)	(9,347)	(1,231)

*Excludes money market.

Source: Morningstar Direct Asset Flows.

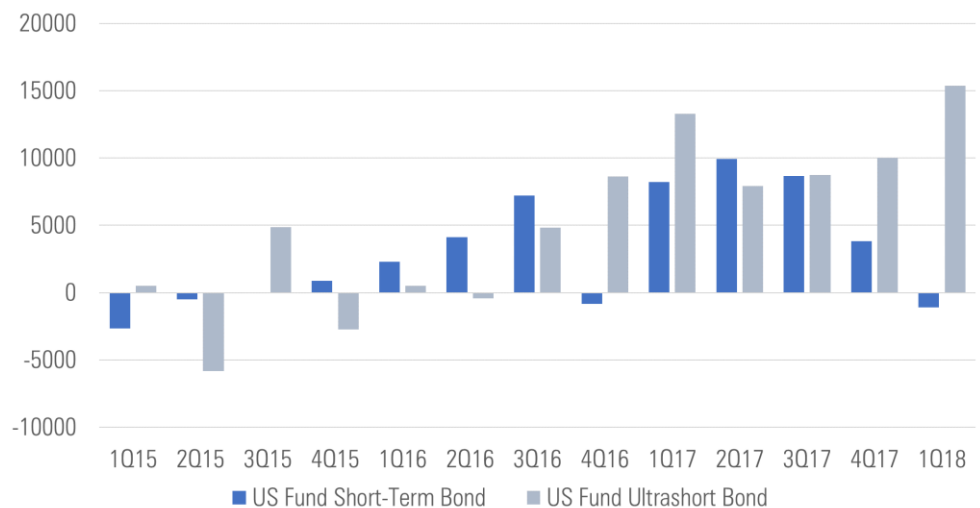
Taxable-bond funds fared even better in absolute terms, bringing in \$25.3 billion, the second consecutive monthly increase and roughly on par with their trailing three-year run-rate. Ultrashort bond funds, which typically have average durations of less than one year, had the greatest inflows — \$5.6 billion — as Federal Reserve interest-rate hikes boosted the yields on offer. iShares Short Treasury

Bond ETF SHV, which took in \$2.5 billion in April, has a current SEC yield of 1.75%, although this is lower than the 1.85% for Vanguard Prime Money Market Fund VMMXX.

A bit more surprising, the average intermediate-term bond fund took in nearly \$5 billion in April, even as the typical fund in the group fell 1.93% for the year to date through April due to rising rates. Even more surprising, the long government category collected \$3.4 billion, despite losing 2% on average in April alone and 5.3% year-to-date.

Investors could be trying to diversify away their equity risk. In recent decades, long-term Treasuries have had a negative correlation with U.S. equities, making them an ideal hedge. However, they haven't served that function recently, as rising rates have hurt bonds as well as equities.

Exhibit 3 As Rates Rise, Investors Prefer Ultrashort Bond Funds (\$ Mil.)



Source: Morningstar Direct Asset Flows.

Meanwhile, short-term bonds didn't get much love from investors. Their flows were flat in April (although short-government funds did collect \$1.0 billion), despite the average fund being down just 0.37% year-to-date, far better than the showing for intermediate-term or long-government funds. The same held true for municipal-bond funds. Muni national short funds had that group's greatest outflows (\$1.4 billion), despite being down just 0.22% year-to-date. Conversely, muni-national long funds had less than \$300 million in outflows, despite being down 1.7% year-to-date.

Sector funds had outflows of \$9.2 billion, the greatest exodus in at least 10 years. Healthcare funds had outflows of \$1.6 billion followed by withdrawals of \$1.4 billion from real-estate funds. Health funds have been volatile recently, but remain up 1.7% on average year-to-date. Real-estate funds, on the other hand, have been stung by rising rates and weak results within the retail subsector, thanks in part to competition from Amazon.com AMZN, and are down 6% on average. Hardly any sector categories were

spared. Even equity energy funds, which are up nearly 10.1% on average in 2018, saw about \$650 million in net redemptions.

Exhibit 4 Top 10 U.S. Fund Families by Assets Under Management

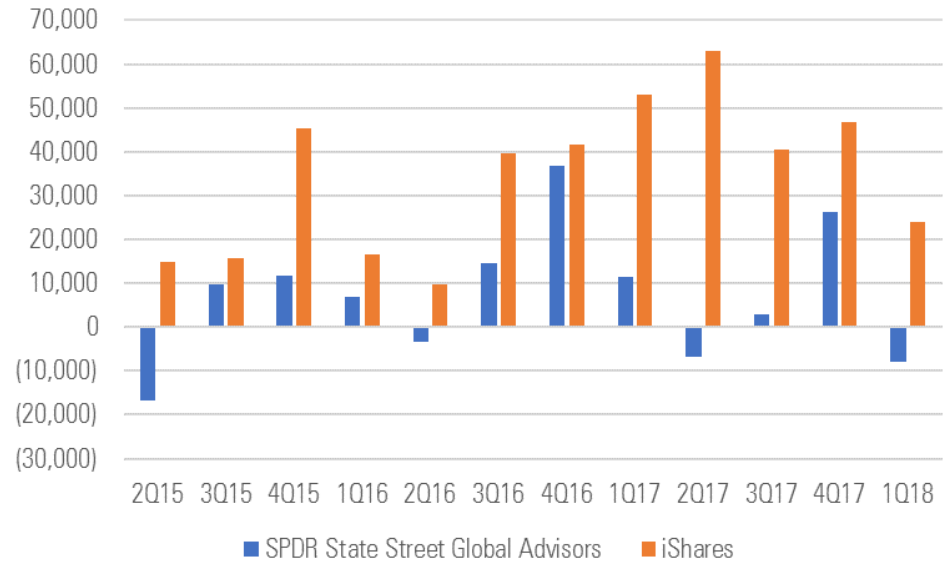
Estimated Net Flows \$Mil	April Flows			Total 1 Year Total	Assets \$Bil
	Active	Passive			
Vanguard	(2,163)	14,491	12,328	275,747	4,359
American Funds	2,412		2,412	24,908	1,547
Fidelity Investments	(11,182)	5,713	(5,469)	24,405	1,470
iShares	487	16,479	16,966	167,666	1,369
SPDR State Street Global Advisors	256	3,254	3,510	23,897	606
T. Rowe Price	1,209	(241)	968	(10,991)	601
Dimensional Fund Advisors	1,794	40	1,834	28,872	412
Franklin Templeton Investments	(2,768)	2	(2,766)	(28,673)	371
PIMCO	1,500	(122)	1,378	33,776	357
JPMorgan	634	135	769	9,647	304

Source: Morningstar Direct Asset Flows.

Vanguard was near the top of the fund-family league tables with \$12.3 billion in inflows. But BlackRock's iShares eclipsed that figure with about \$17 billion in inflows. Vanguard's year-to-date growth continues to slow year over year. Through the first four months of 2017, Vanguard took in an estimated \$141.5 billion. So far in 2018, the firm has only collected about half that amount, \$71 billion. The firm's one-year organic growth rate of 7.4% is less than half of iShares' 15.1%. This slowing growth shouldn't be surprising given that Vanguard is more than triple iShares' size, but it's notable since Vanguard defied the odds, growing at scale in recent years, a rare anomaly.

While iShares Short Treasury Bond led the way in April, so far in 2018 iShares Core MSCI EAFE IEFA and iShares Core MSCI Emerging Markets IEMG lead the firm year-to-date with inflows of \$16.4 billion and \$8.0 billion, respectively.

The contrast with SPDR State Street Global Advisors is striking. Both firms were ETF pioneers, but iShares continues to separate itself from its rival. Over the past 12 months, iShares has collected about \$168 billion versus just \$24 billion for SPDR funds. As a result, while SPDR's market share is basically flat over that span at 3.34%, iShares' has grown to 7.54% from 6.93%. As mentioned last month, SPDR falls short on cost relative to offerings from iShares and others. This is having a meaningful impact on investor demand.

Exhibit 5 Three-Year Flows for iShares and SPDR ETFs (\$ Mil.)

Source: Morningstar Direct. Data as of 28 March 2018.

Even more active-oriented fund families received most of their inflows from passive funds. Fidelity had overall outflows of about \$5.6 billion, its worst month since November 2016. However, these outflows were mostly on the active side of the house, which shed about \$11.3 billion in net redemptions, while the firm collected about \$5.7 billion in passive flows.

Franklin Templeton continues to see outflows, with another \$2.8 billion walking out the door in April. The firm has now lost nearly \$29 billion to outflows over the past 12 months. Allocation fund Franklin Income FKINX has endured nearly \$6.2 billion in redemptions alone over the past 12 months.

Exhibit 6 Bottom-Flowing Funds

Bottom Funds	Estimated Net Flow (\$Mil)		
	April 2018	1 Year	Assets
Fidelity® Large Cap Stock Fund	(1,282)	(1,315)	3,871
Fidelity® Select Technology Portfolio	(1,188)	(349)	5,895
Fidelity® Value Discovery Fund	(1,183)	(144)	2,478
Vanguard Institutional Index Fund	(1,152)	(34,342)	220,001
Fidelity® Contrafund® Fund	(980)	(6,306)	124,116
iShares MSCI EAFE ETF	(888)	372	78,401
JPMorgan Corporate Bond Fund	(805)	(1,898)	88
Consumer Staples Select Sector SPDR®	(750)	(372)	7,561
Fidelity® Series Investment Grade Bond	(706)	2,646	27,647
Harbor International Fund	(651)	(11,719)	26,197

Source: Morningstar Direct Asset Flows.

Exhibit 7 Top-Flowing Funds

Top Funds	Estimated Net Flow \$Mil		
	April 2018	1 Year	Assets
Vanguard Total Stock Market Index Fund	4,376	45,658	679,304
iShares Short Treasury Bond ETF	2,525	9,031	13,847
Vanguard Total Intl Stock Idx Fund	2,175	34,170	346,564
Fidelity® Total Market Index Fund	2,030	4,899	51,767
iShares Core MSCI Emerging Markets ETF	1,834	16,710	50,930
iShares Core S&P 500 ETF	1,828	20,622	142,639
iShares Core MSCI EAFE ETF	1,811	31,100	58,828
Vanguard 500 Index Fund	1,797	46,915	403,945
iShares 20+ Year Treasury Bond ETF	1,696	1,347	7,851
iShares Core US Aggregate Bond ETF	1,628	13,201	55,830

Source: Morningstar Direct Asset Flows.

Note: The figures in this report were compiled on April 16, 2018, and reflect only the funds that had reported net assets by that date. The figures in both the commentary and the extended tables are survivorship-bias-free.

This report includes both mutual funds and exchange-traded funds, but not funds of funds unless specifically stated. It does not include Collective Investment Trusts (CITs) or separate accounts.

Important methodology note: Morningstar computes flows using the approach that is standard in the industry: Estimated net flow is the change in assets not explained by the performance of the fund. Our method assumes that flows occur uniformly over the course of the month. Adjustments for mergers are performed automatically. When liquidated funds are included, the final assets of the fund are counted as outflows. Reinvested dividends are not counted as inflows. We use fund-level reinvestment rates to improve accuracy in this respect. We make ad hoc adjustments for unusual corporate actions such as reverse share splits, and we overwrite our estimates with actual flows if managers are willing to provide the data to us. Please click [here](#) for a full explanation of our methodology.



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