February 6, 2004

Monthly Mutual Fund Report - 2003 Review

Statistics for December 2003 - January 2004

After experiencing outflows in 2002 for the first time in 14 years, equity funds had strong net inflows in 2003. While bond fund cash flow remained positive for the full year, flows turned negative in July due to increasing interest rates and remained negative throughout the rest of the year. The low interest rates on short-term investment led to larger money market outflows than in 2002, according to the Investment Company Institute.

Sales and Redemptions

Total assets for all funds increased in December by $178.9 billion, or 2.5 percent, to $7.41 trillion. Money market funds had a net cash outflow of $22.8 billion compared to an outflow in November of $7.6 billion. Other funds (equity, hybrid, and bond) had a net cash inflow of $15.6 billion, compared to an inflow of $15.3 billion in November. New sales of non-money market funds, the purchase of new shares excluding reinvested dividends, were $128.1 billion in December, up from $107.6 billion in November. The value of non-money market assets appreciated by $164.6 billion in December, following an appreciation of $71.1 billion in November.

Total assets of **equity funds** increased by $169.6 billion, or 4.8 percent, to $3.68 trillion. There was a $14.7 billion net cash inflow to equity funds in December, compared with an inflow of $14.9 billion in November. The market value of assets appreciated by $143.8 billion in December. In 2003, equity funds had a $152.7 billion inflow, compared to an outflow of $27.7 billion in 2002.

Total assets for **hybrid funds**, which invest in a mix of stocks and bonds, increased 4.8 percent, or $20.2 billion, to $436.6 billion. In December, there was a $3.7 billion net cash inflow for these funds. In 2003, hybrid funds had a $33.2 billion inflow, while there was a $8.6 billion inflow in 2002.

Bond funds experienced a cash outflow of $2.8 billion, while their total assets increased by $8.1 billion, to $1.24 trillion. The market value of bond funds assets increased by $6.7 billion, after adjusting for net sales and reinvested dividends. The assets of taxable bond funds increased by 0.9 percent, while the assets of tax-exempt bond funds increased by 0.1 percent. The 2003 inflow to bonds was $31.4 billion; in 2002, the total inflow was $140.3 billion.

Assets of taxable and tax-exempt **money market funds** decreased $19.0 billion, to $2.05 trillion, a decrease of 0.9 percent for taxable money market funds and a decrease of 1.3 percent for tax-exempt funds. Compared to a net cash outflow of $46.7 billion in 2002, money market funds had an outflow of $259.0 billion in 2003.

Liquidity Ratio

The liquidity ratio for bond and hybrid funds increased from 6.03 to 6.05 percent, while the ratio for equity funds decreased from 4.59 to 4.26 percent (figure 4).

Weekly Flows

In January, there were inflows to equity funds of 0.2 percent of total assets, with returns of 3.6 percent (figure 6). January's inflow was the largest as a percent of total assets for any month since March 2002, which was a temporary spike amid large monthly outflows. A better comparison can be made to the end of 2000, the last time equity fund inflows remained positive for any amount of time, as they have for the last four months.

Bond funds had inflows of 0.4 percent and returns of 0.5 percent for the month. Index funds had monthly inflows of 0.01 percent and returns of 3.4 percent. Aggressive growth funds had monthly inflows of 0.4 percent and returns of 4.2 percent. Small-cap funds had an inflow of 2.0 percent and returns of 3.0 percent.

There were inflows to international funds in January of 0.8 percent of assets and returns of 4.6 percent. Latin America funds had inflows of 0.2 percent and returns of 6.9 percent. Japan funds had outflows of 6.1 percent and returns of 2.6 percent of assets for the month of January. Pacific funds that do not invest in Japan had outflows of 3.5 percent and returns of 4.5 percent of assets.

Capital Market Returns and Volatility

The S&P 500 ended January at 1131.13, an increase of 1.7 percent from the beginning of the month. The 12-month gain was 35.2 percent at month-end. The annualized volatility for the daily return on the S&P 500 was 15.9 percent.

The 12-month average return on the Citigroup Bond Index was 5.0 percent for January. Volatility increased to 5.28 percent (figure 8).

Price-Earnings Ratio

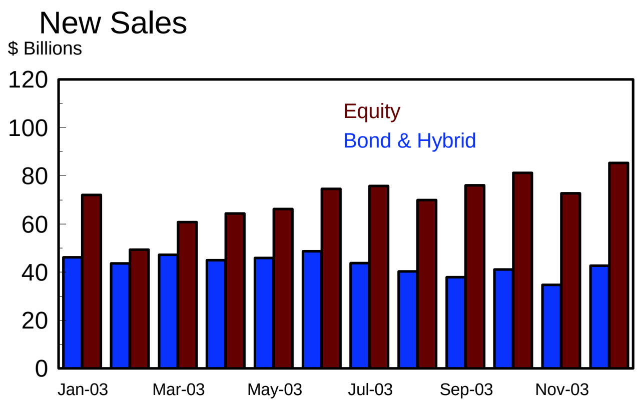
The macro projections for the growth of earnings of the Standard and Poor’s 500 index over the next two years have decreased in the fourth quarter to 2.5 percent, below the 6.6 percent historical average annual growth rate. The trailing price-earnings ratio decreased from 25.8 in the third quarter to 24.6 for the fourth quarter of 2003, while Thomson Financial/First Call's forward price-operating earnings was 18.1 in the first quarter of 2004, unchanged from the fourth quarter of 2003 (figure 9). During the fourth quarter the price-earnings ratio for the Standard and Poor's Small-Cap 600 Index rose to 30.8 from 29.6.

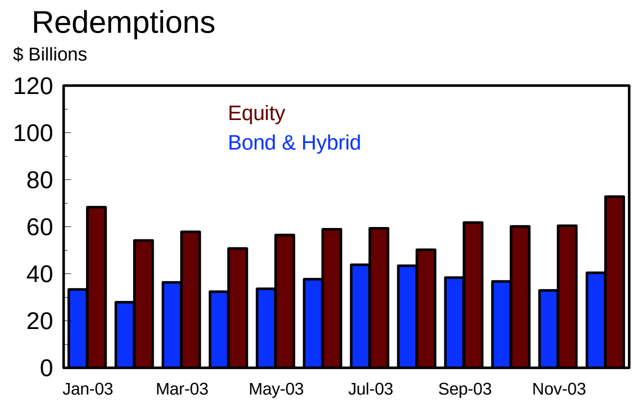
The Monthly Mutual Fund Report is available online at http://www.bos.frb.org/economic/mmfr/mmfr.htm.

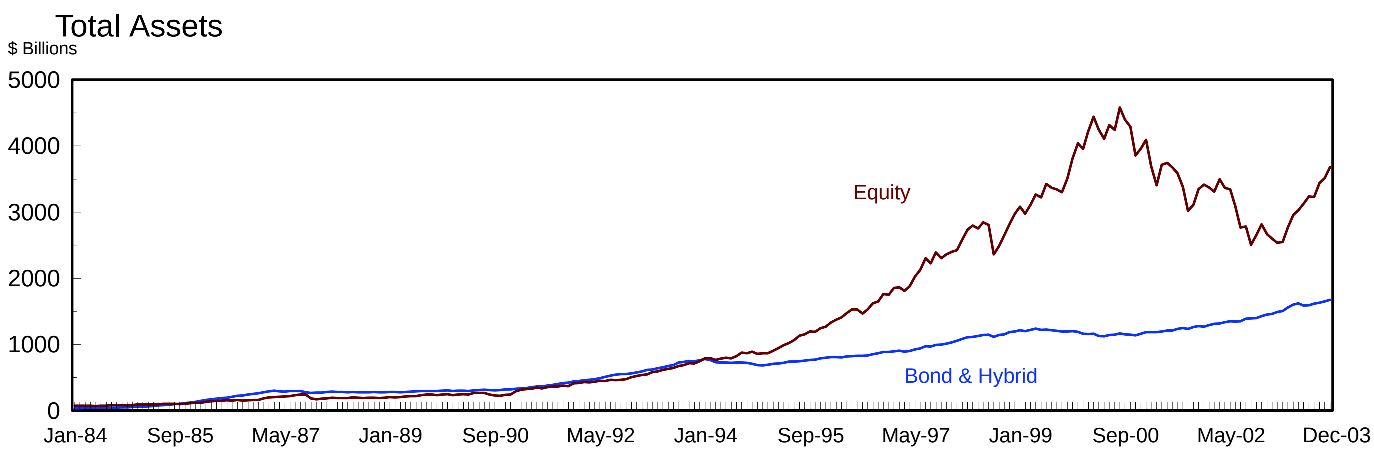
Also, the Stock Market Report is now available to the general public. The current issue, as well as previous editions, can be found at our public website, http://www.bos.frb.org/economic/smr/smr.htm.

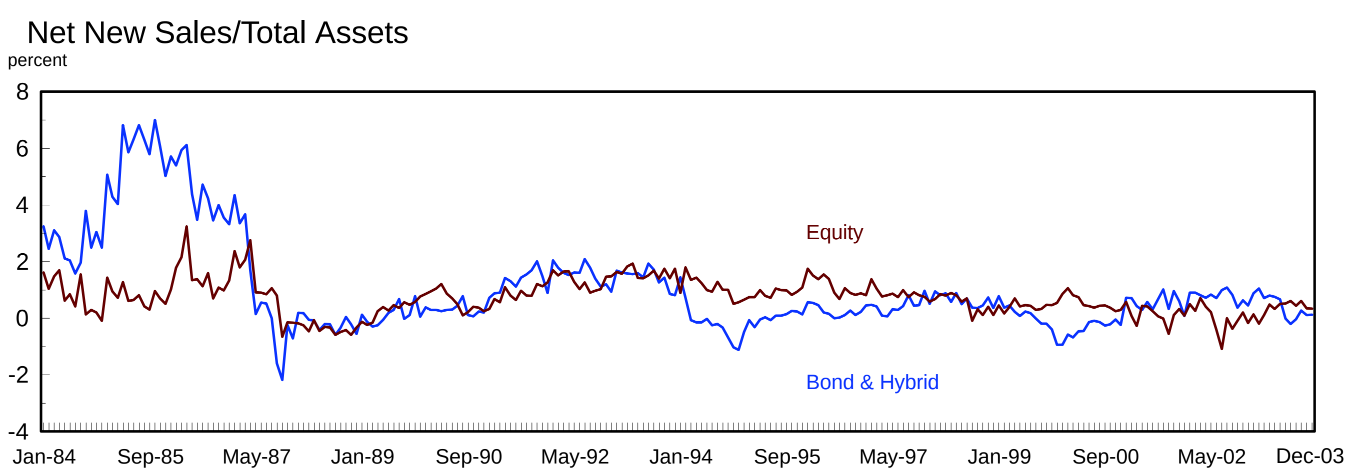
Please contact Matthew S. Rutledge for questions and comments at Matthew.S.Rutledge@bos.frb.org, or by phone at (617) 973-3198.

Figure 1
Sales of Mutual Funds







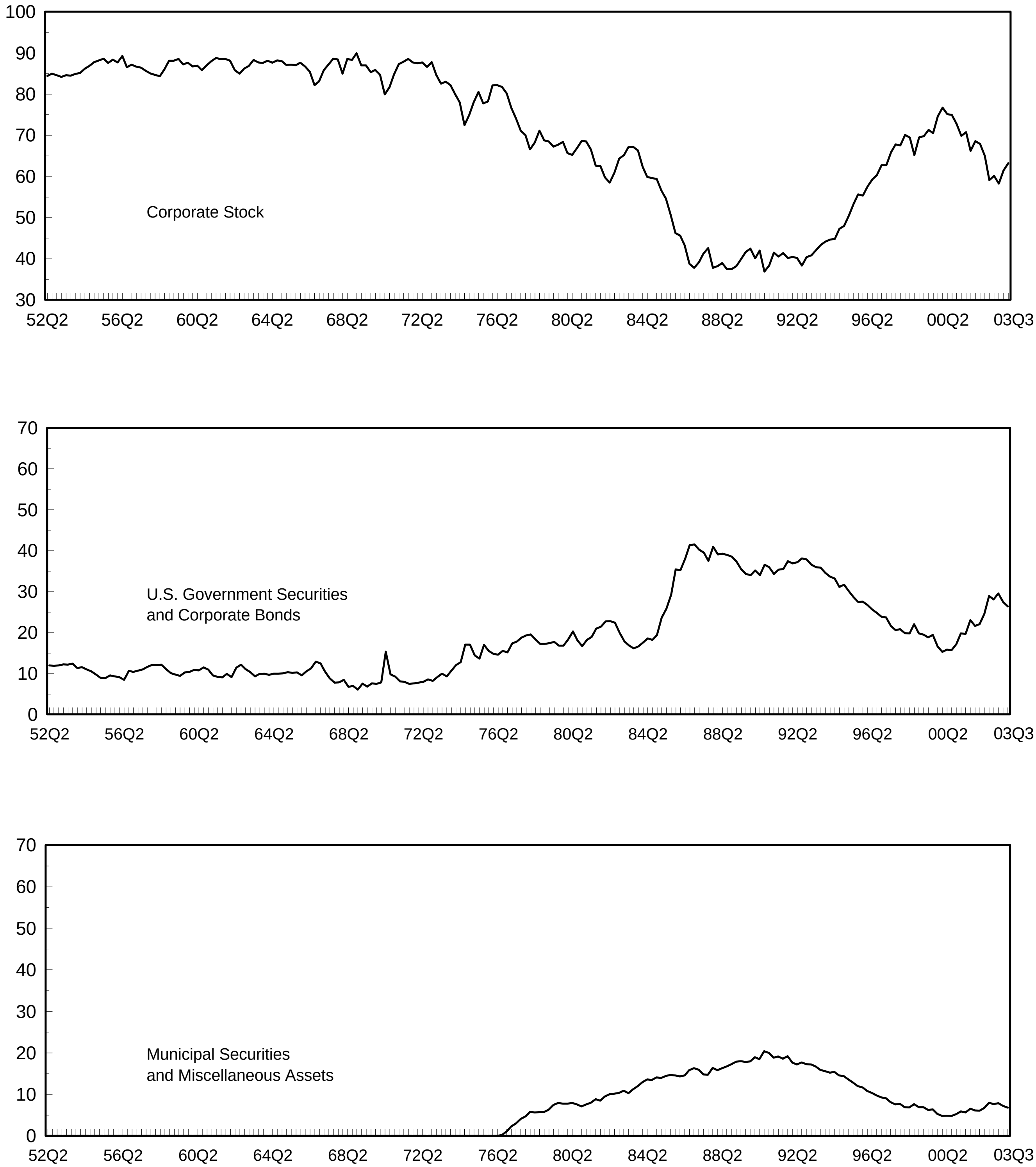


Source: Investment Company Institute

Figure 2

Composition of Mutual Funds' Financial Assets

(percent of Total Financial Assets)

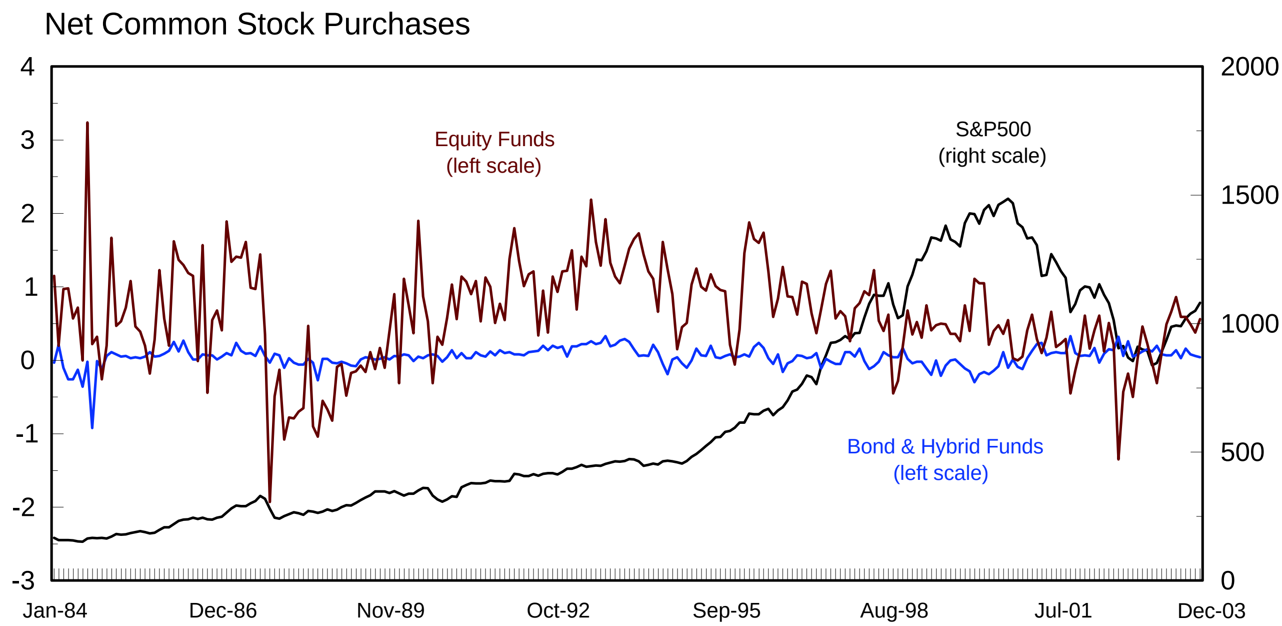


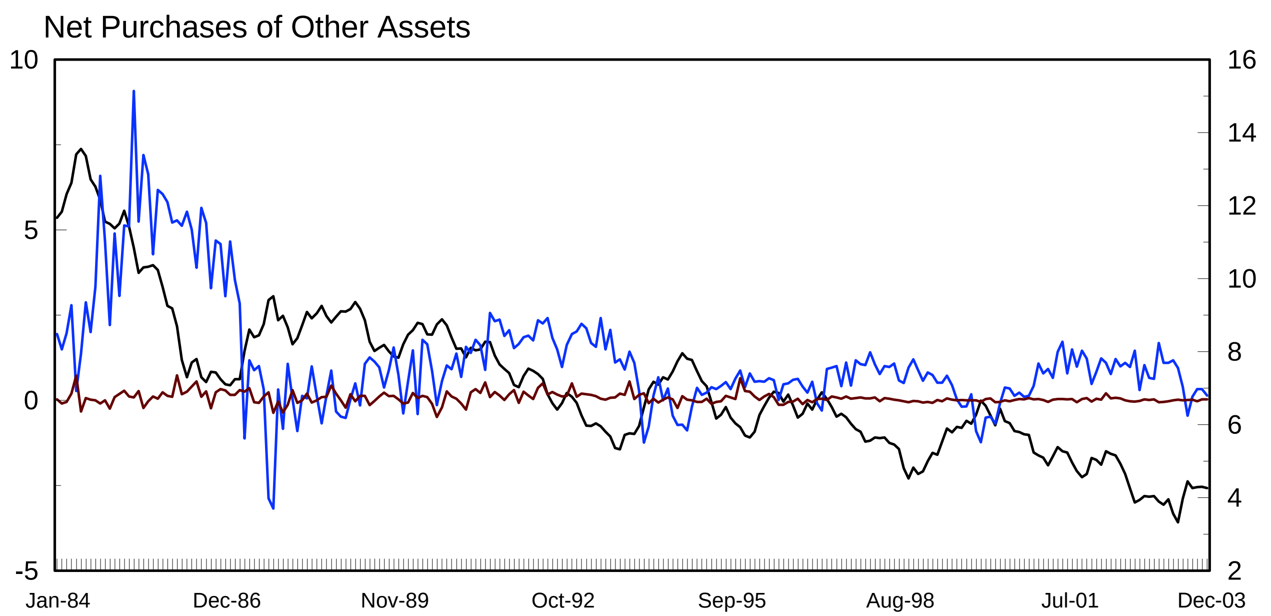
Source: Flow of Funds, Haver Analytics

Figure 3

Net Portfolio Purchases

(percent of Total Assets)

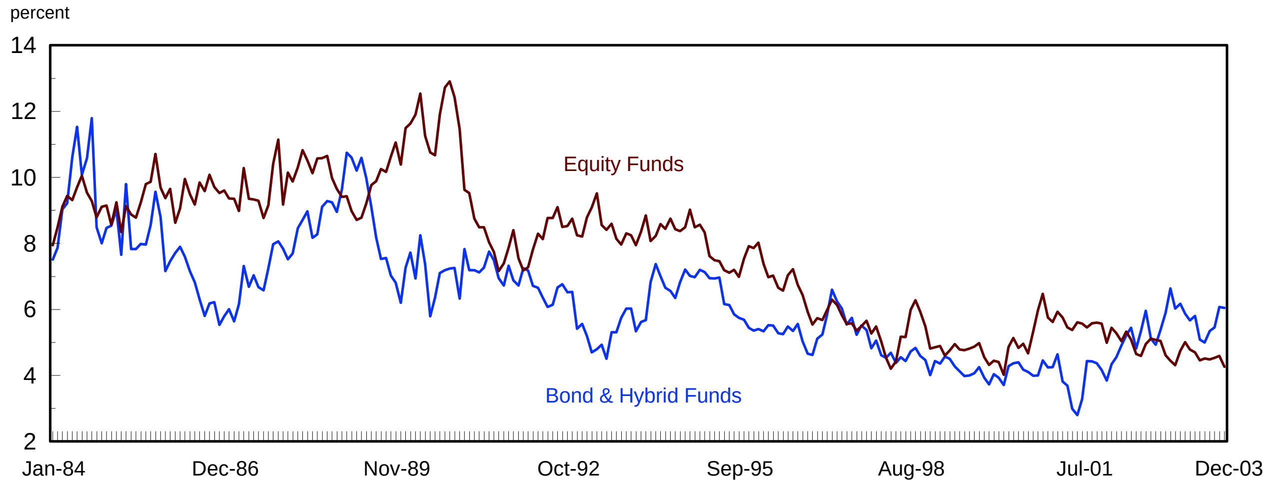




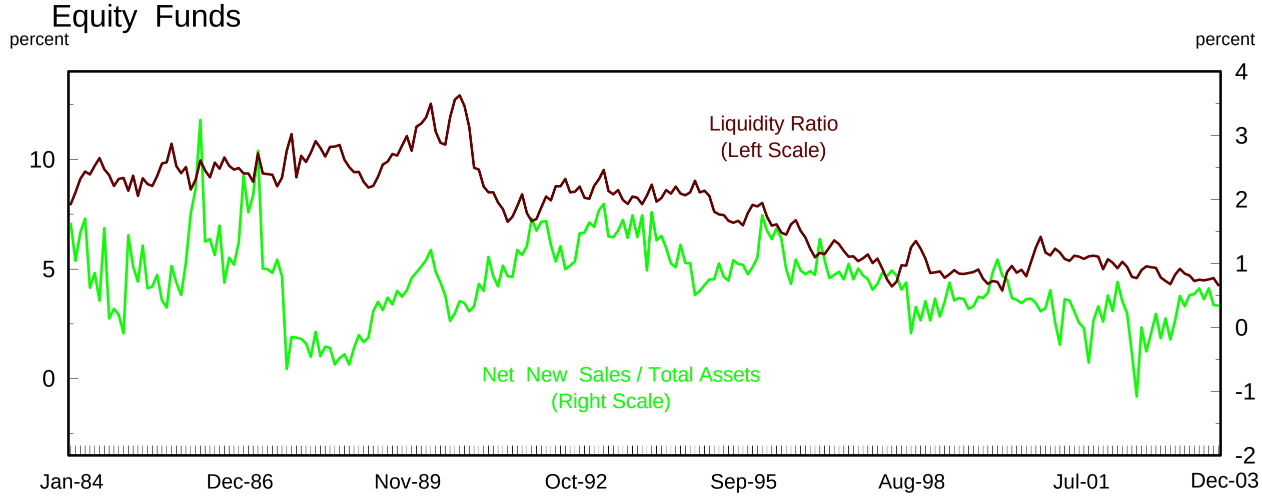
Source: Investment Company Institute

Figure 4

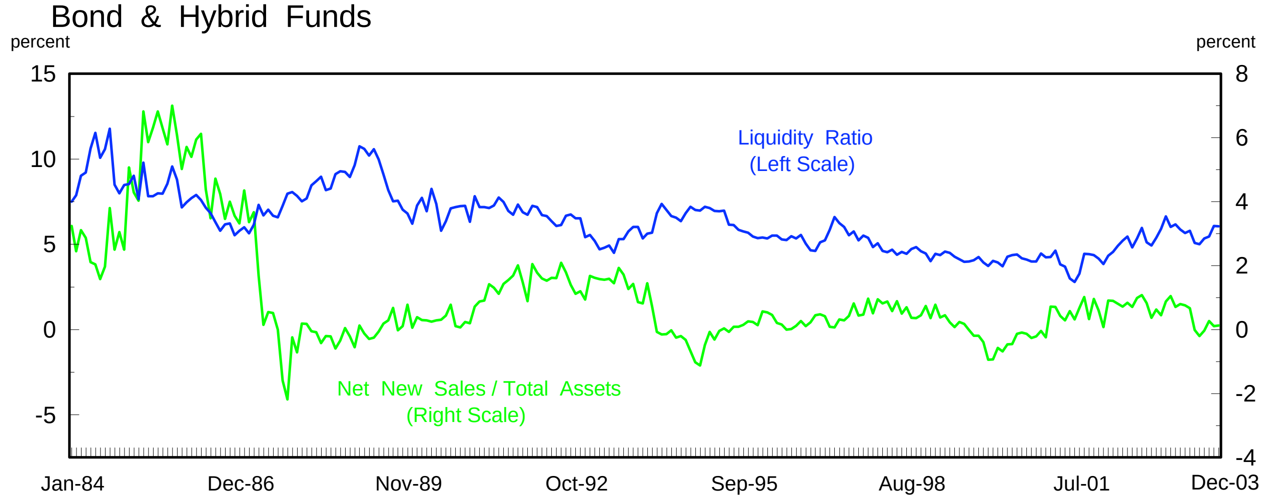
Liquidity Ratio*



Equity Funds



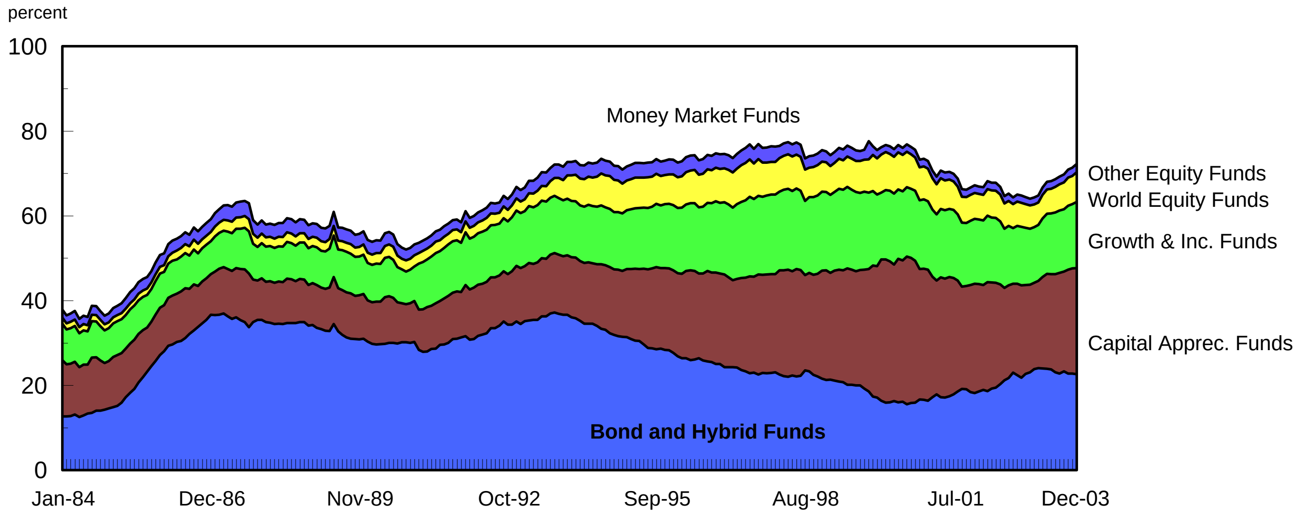
Bond & Hybrid Funds



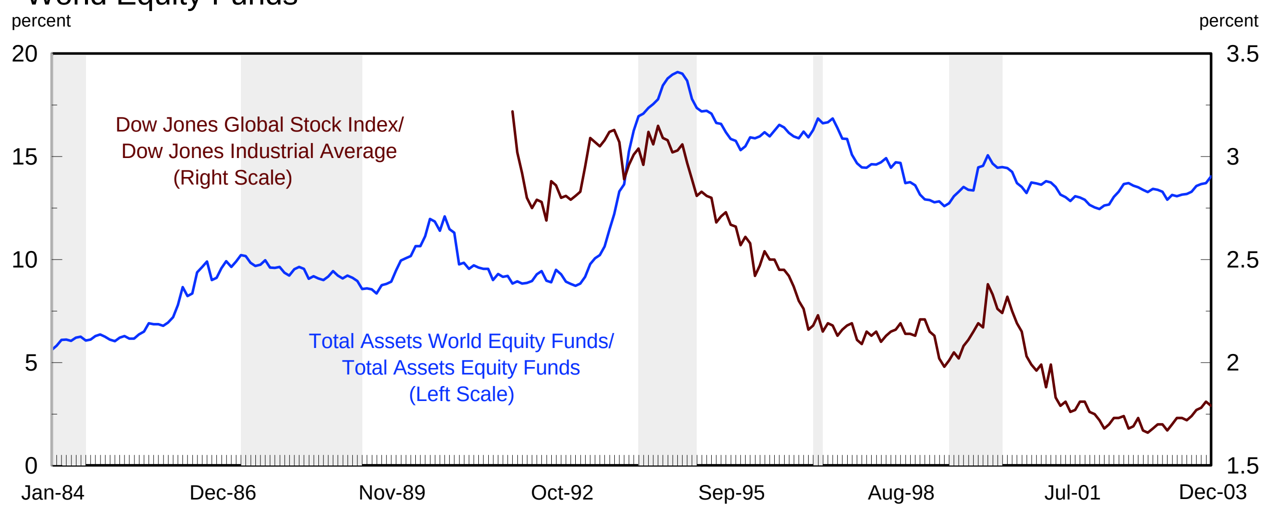
*The Liquidity Ratio is the Percent of Total Assets held in Cash and Short-Term Securities.

Source: Investment Company Institute

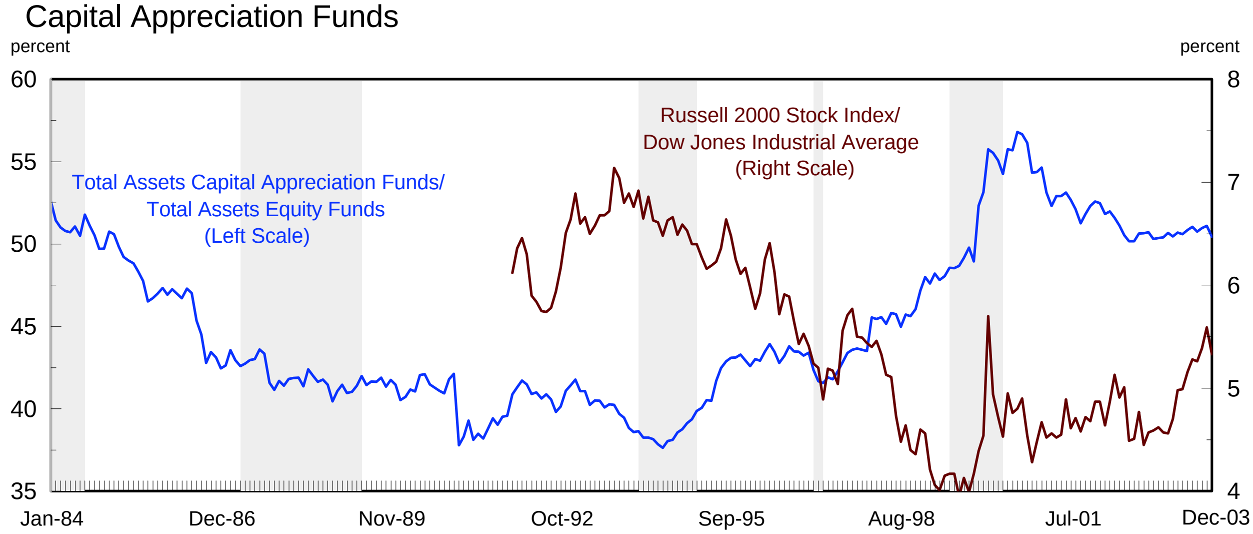
Figure 5
Industry Composition
(Shaded Regions Indicate Periods of Rising Fed Funds Rate)



World Equity Funds



Capital Appreciation Funds

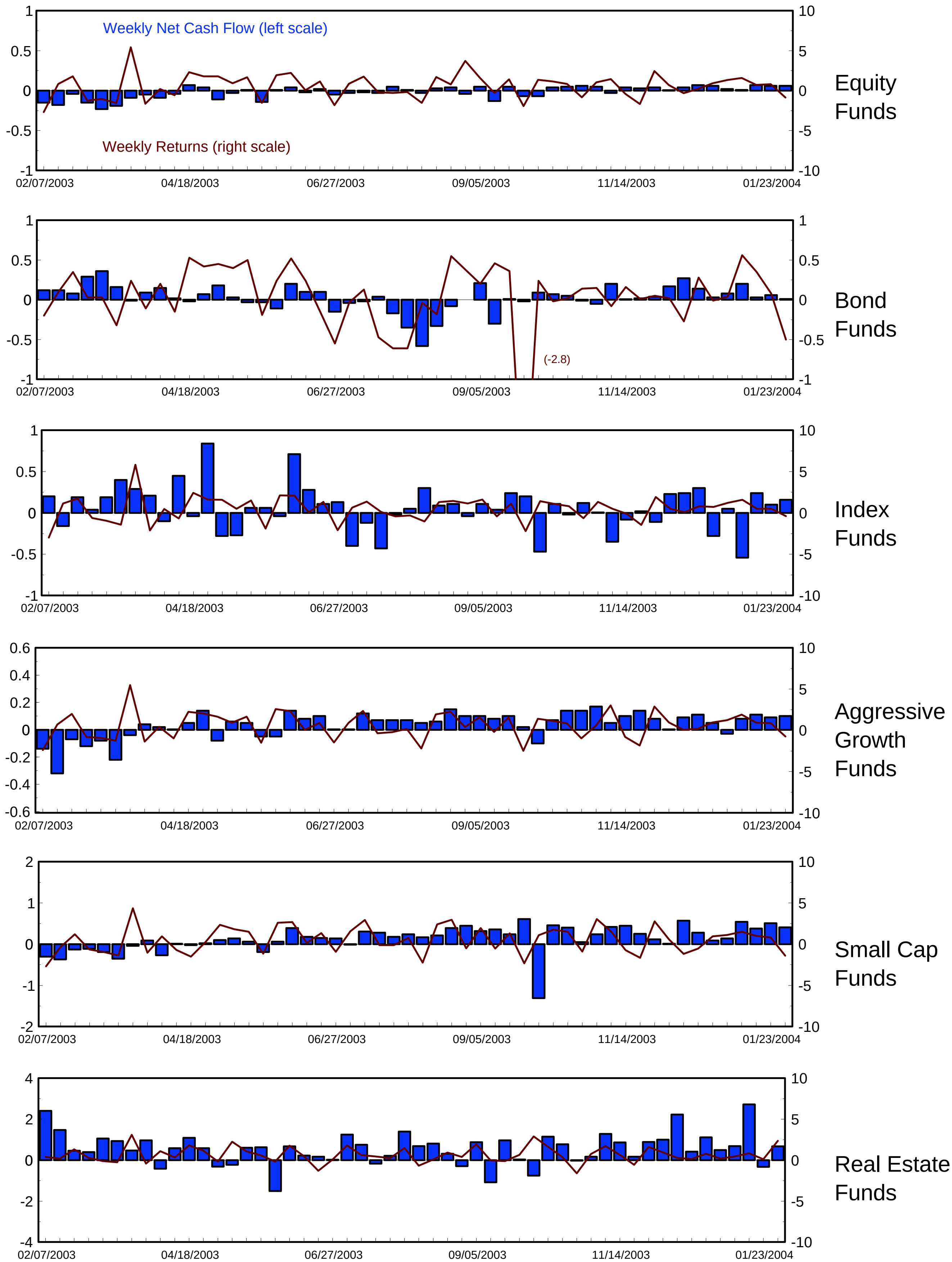


Source: Investment Company Institute

Figure 6a

Weekly Flows into Mutual Funds

(percent of Total Assets)

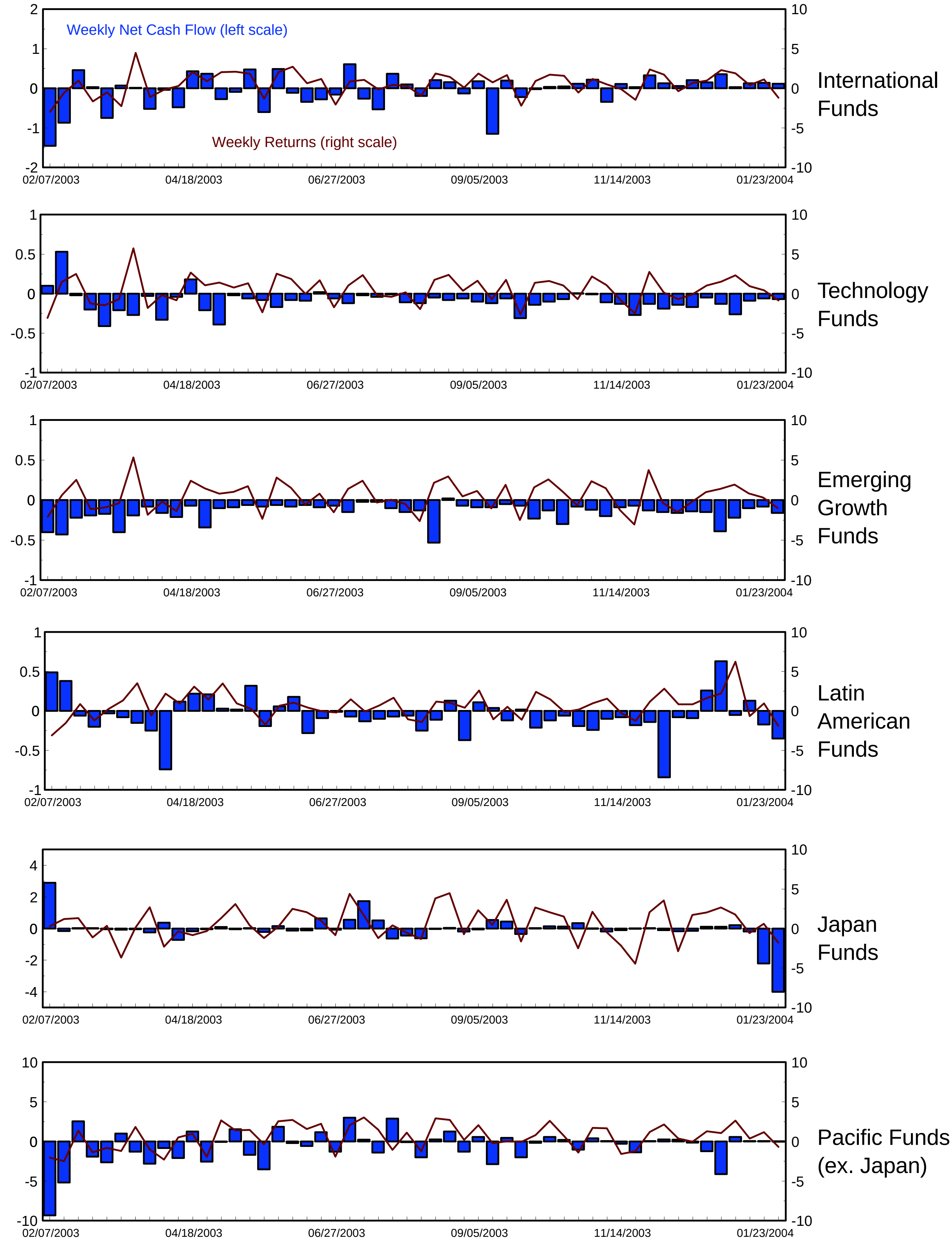


Source: Mutual Fund Trim Tabs

Figure 6b

Weekly Flows into Mutual Funds

(percent of Total Assets)

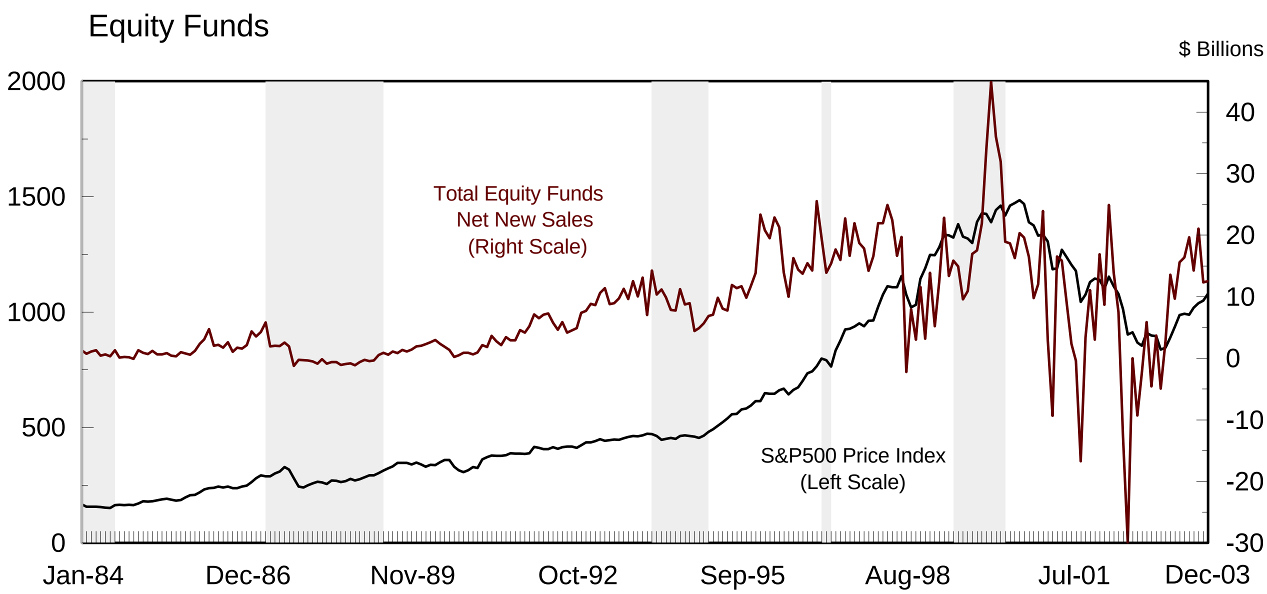


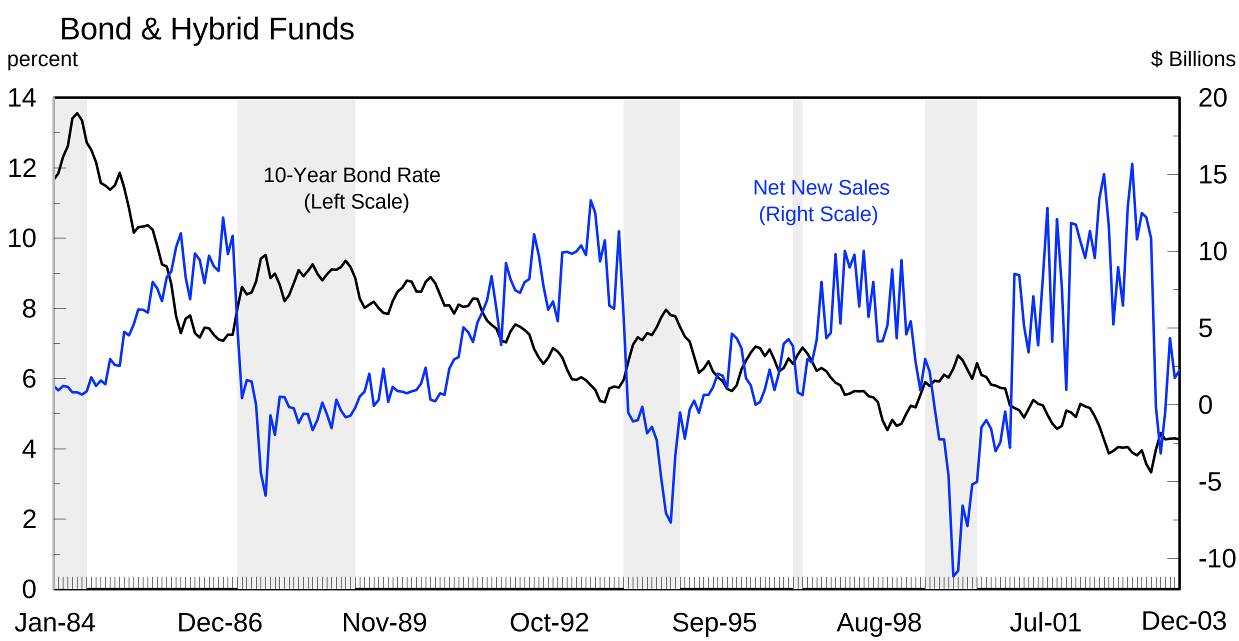
Source: Mutual Fund Trim Tabs

Figure 7

Net New Sales By Investment Objective

(Shaded Regions Indicate Periods of Rising Fed Funds Rate)

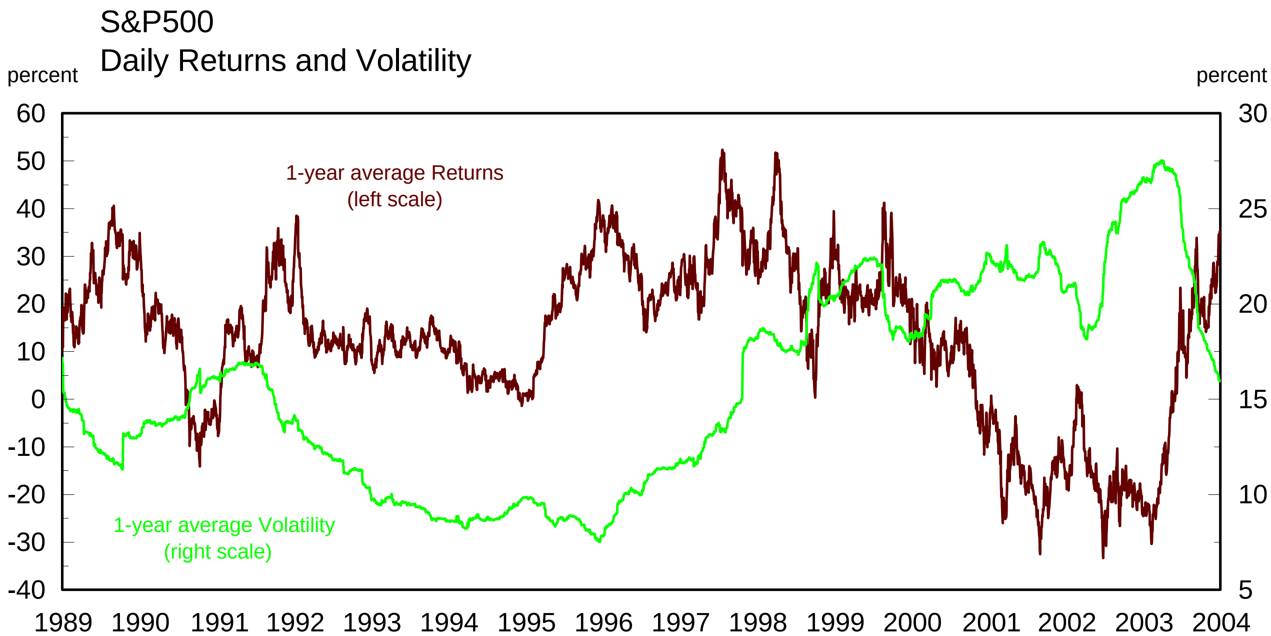


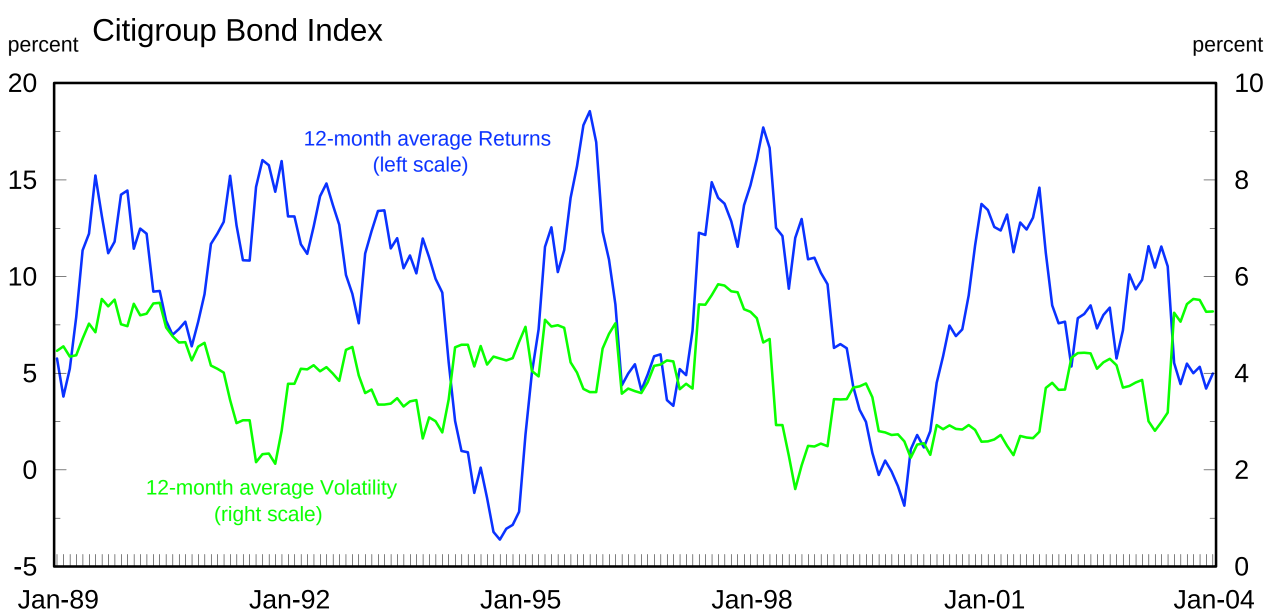


Source: Investment Company Institute

Figure 8

Capital Market Returns and Volatility

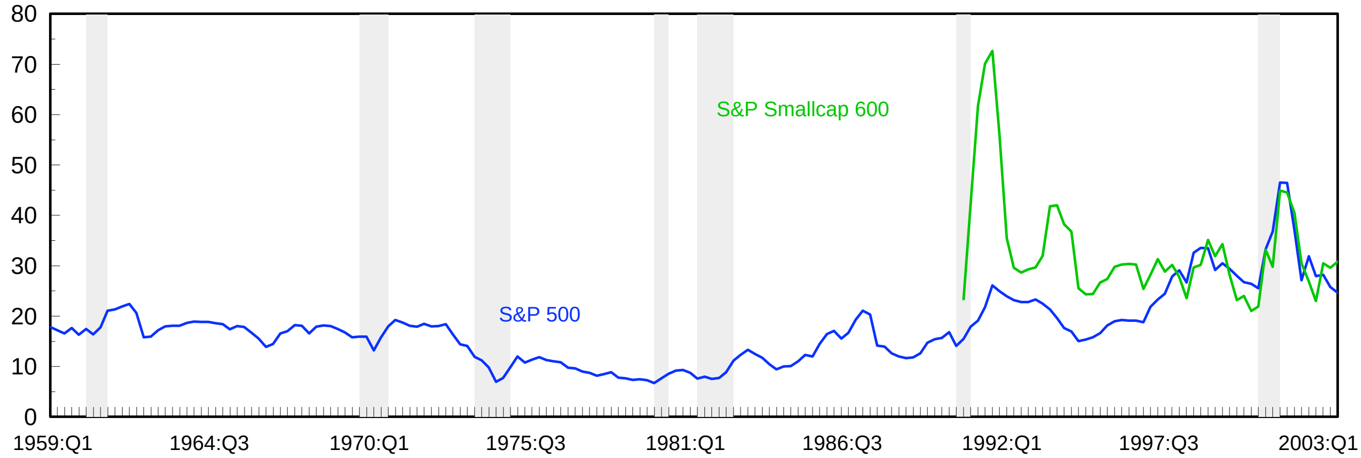




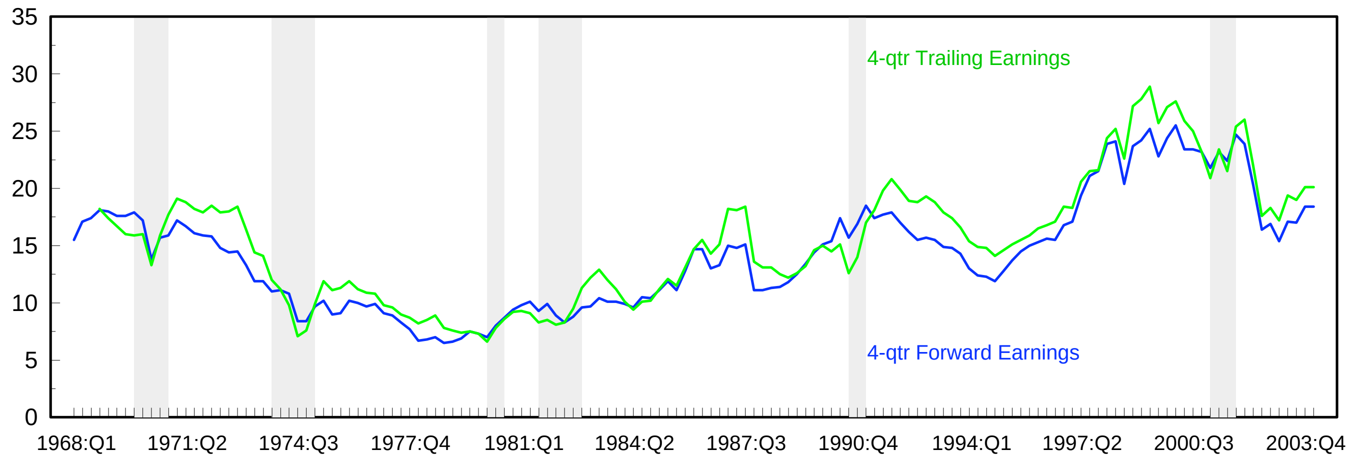
Source: FAME Database, Citigroup

Figure 9

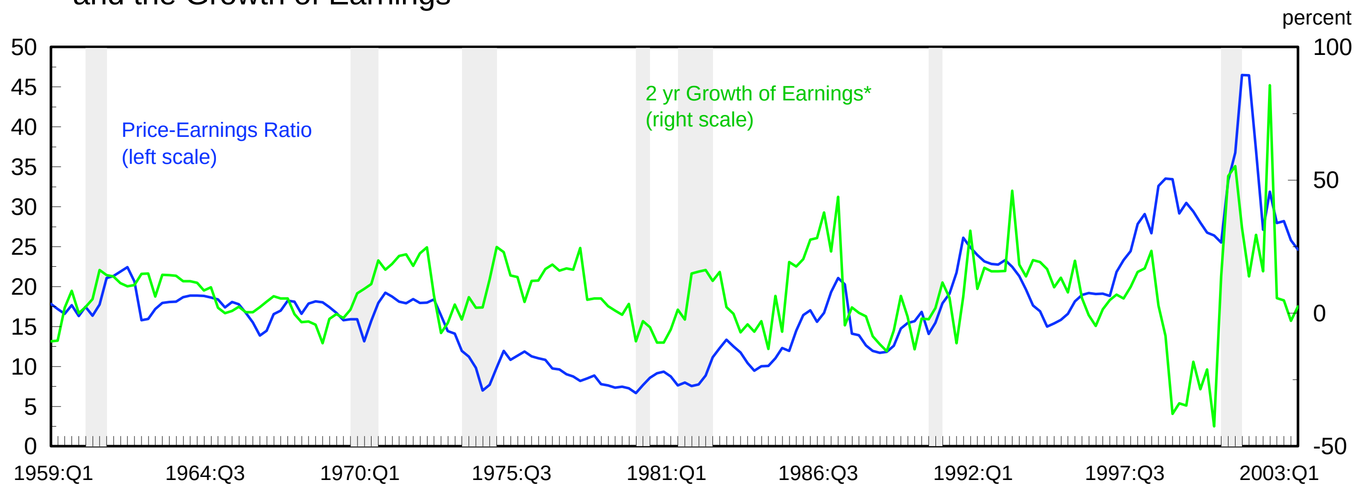
S&P Price-Earnings Ratios



S&P500 Price-Operating Earnings Ratio



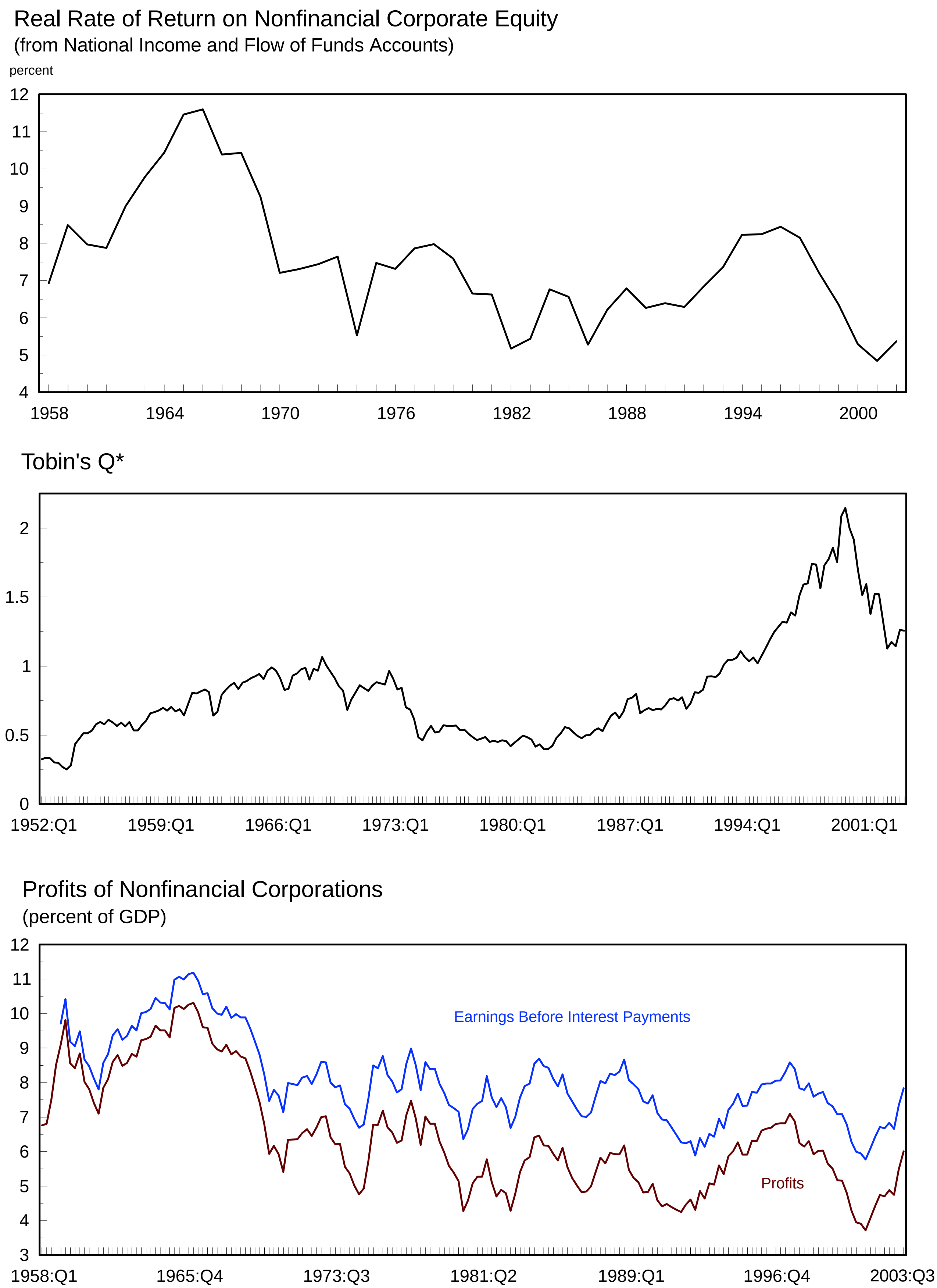
S&P500 Price Earnings Ratio
and the Growth of Earnings



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

source: Thomson Financial/First Call, Global Exchange (formerly DRI), Bloomberg

Figure 10



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

Source: Flow of Funds, Haver Analytics