

## Morningstar Direct<sup>SM</sup> Asset Flows Commentary: United States

**Morningstar Research**  
**18 January 2018**

Data through Dec. 31, 2017  
 U.S. Mutual Funds and Exchange-  
 Traded Products

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### Taxable Bond and International Equity Dominated Flows in 2017

Investors displayed an overwhelming preference for taxable-bond and international-equity funds last year. As the U.S. stock bull market is fast approaching its nine-year anniversary, two trends have become predominant: rebalancing from stocks to bonds, and diversifying stock allocations internationally.

Taxable-bond funds were by far the most popular Morningstar category group in terms of active flows, demonstrating that an active manager's skill in fixed income is still valued. On the flip side, active U.S. equity was the most unpopular category group, with a \$207 billion outflow in 2017. The two other category groups with negative flows on the active side were allocation and sector equity.

U.S. equity shone on the passive side, with inflows of \$220 billion. Investors have been generally maintaining their U.S. equity positions, but switching from high-cost active to low-cost passive. Passive taxable-bond and international-equity funds also received inflows above \$200 billion, as indexing is no longer limited to U.S. equity and expanding into other asset classes.

Estimated Net Flows*	Active			Passive		
	Dec 2017	1 Year	Assets \$ Bil	Dec 2017	1 Year	Assets \$ Bil
U.S. Equity	(16,317)	(207,466)	4,244	22,461	220,373	3,638
Sector Equity	(1,680)	(18,417)	424	3,468	44,185	488
International Equity	1,938	35,621	2,021	17,245	203,784	1,244
Allocation	(7)	(26,825)	1,231	377	3,256	66
Taxable Bond	10,230	178,767	2,611	15,888	210,039	1,096
Municipal Bond	(1,082)	28,673	667	829	5,215	29
Alternative	(677)	1,531	165	(1,411)	3,285	53
Commodities	(215)	1,124	29	(494)	1,450	66
<b>All Long Term</b>	<b>(7,810)</b>	<b>(6,991)</b>	<b>11,393</b>	<b>58,363</b>	<b>691,589</b>	<b>6,680</b>
Money Market	43,788	107,096	2,831			

\*Includes liquidated and merged funds.

Source: Morningstar Direct Asset Flows.

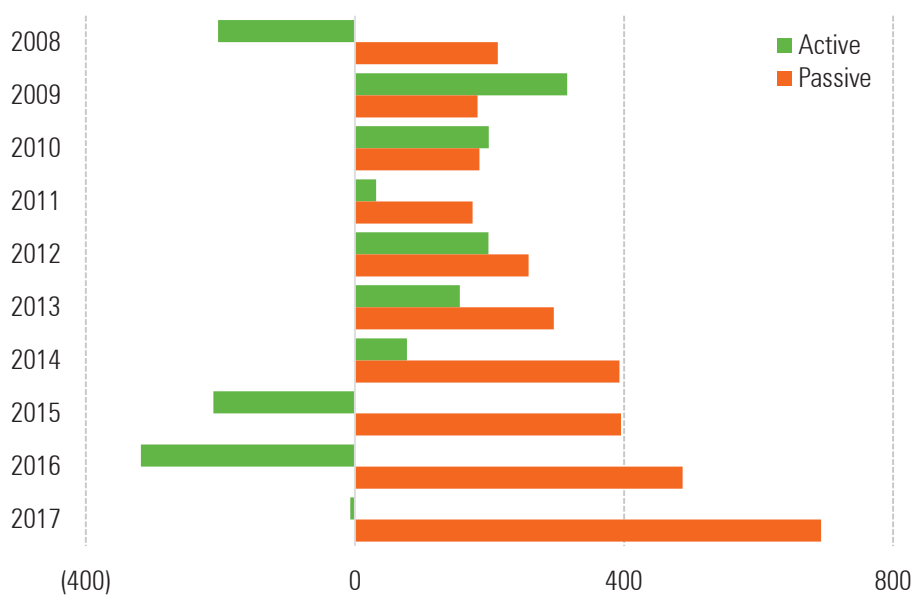
**Total (Active and Passive)**

<b>Estimated Net Flows</b> \$Mil	<b>Dec 2017</b>	<b>1 Year</b>	<b>Assets</b> \$ Bil
U.S. Equity	6,145	12,908	7,882
Sector Equity	1,788	25,768	912
International Equity	19,182	239,406	3,265
Allocation	370	(23,568)	1,297
Taxable Bond	26,118	388,806	3,707
Municipal Bond	(254)	33,888	696
Alternative	(2,088)	4,817	218
Commodities	(709)	2,574	96
<b>All Long Term</b>	<b>50,552</b>	<b>684,598</b>	<b>18,073</b>
Money Market	43,788	107,096	2,831

Source: Morningstar Direct Asset Flows.

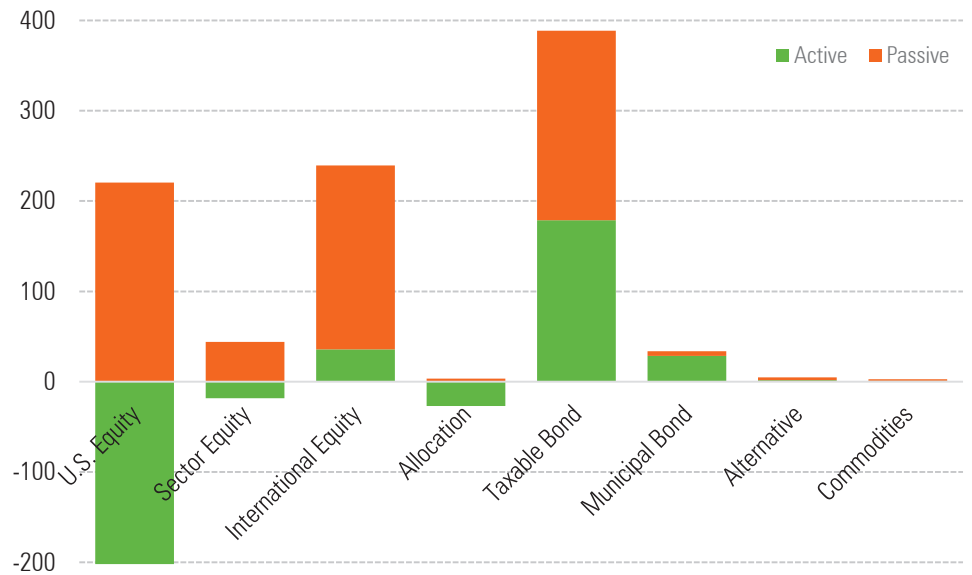
Overall, open-end mutual funds and exchange-traded funds received a record influx of money in 2017: \$684.6 billion. Active funds almost broke even in 2017, which was a relative victory after the extreme outflows of 2015 and 2016. This happened because the total was pulled up by the significant taxable-bond inflow. Without taxable bond, active funds would have suffered a \$185.8 billion outflow.

**Exhibit 1** Flows by Category Group, Active and Passive, for the Past 10 Years (\$ Billion)



Source: Morningstar Direct Asset Flows.

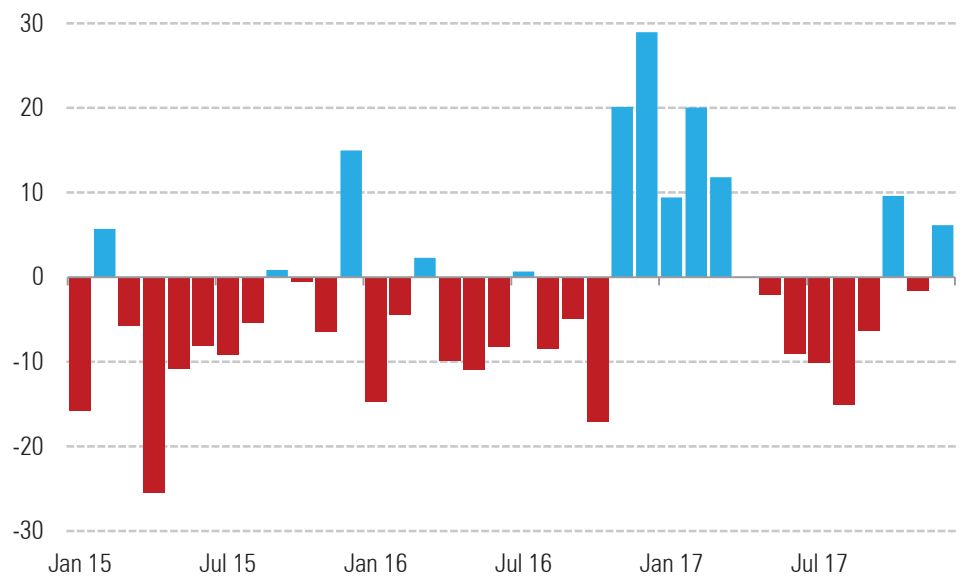
**Exhibit 2** 2017 Flows by Category Group, Active and Passive (\$ Billion)



Source: Morningstar Direct Asset Flows.

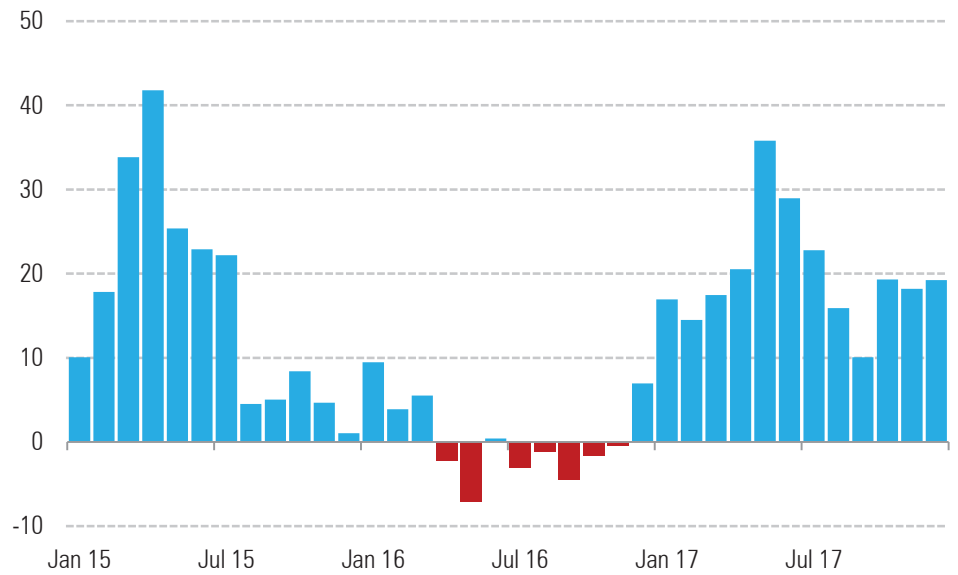
Both U.S. and international stocks had a spectacular year, with the MSCI EAFE Index returning 25.0% and the S&P 500 21.8%. Emerging-markets stocks, which carry additional risk, produced a 37.3% return, their fourth largest since 2001.

**Exhibit 3** U.S. Equity Category Group Monthly Flows (\$ Billion)



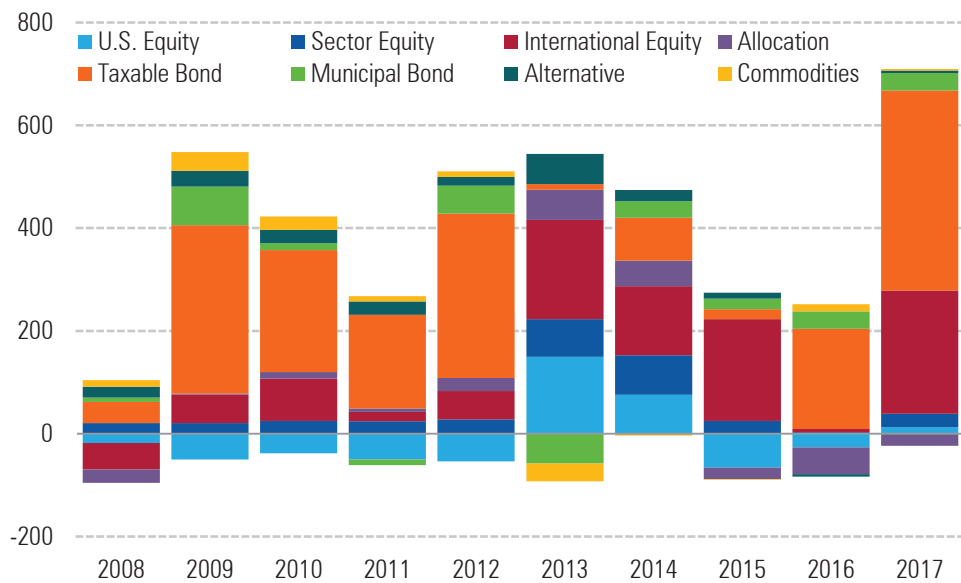
Source: Morningstar Direct Asset Flows.

**Exhibit 4** International-Equity Category Group Monthly Flows (\$ Billion)



Source: Morningstar Direct Asset Flows.

**Exhibit 5** Category Group Flows During the Past 10 Years (\$ Billion)

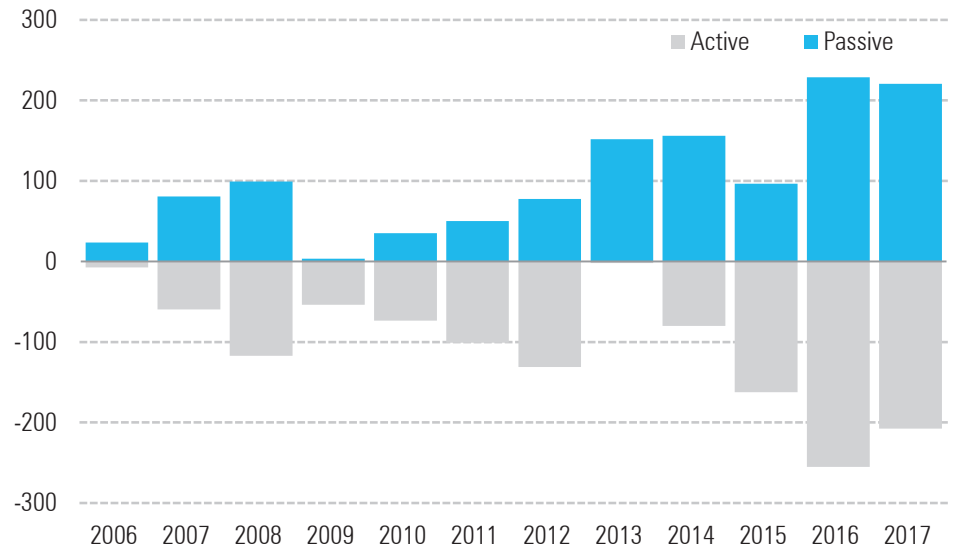


Source: Morningstar Direct Asset Flows.

### The Year in Charts

- Active U.S.-equity flows have been negative since 2006.

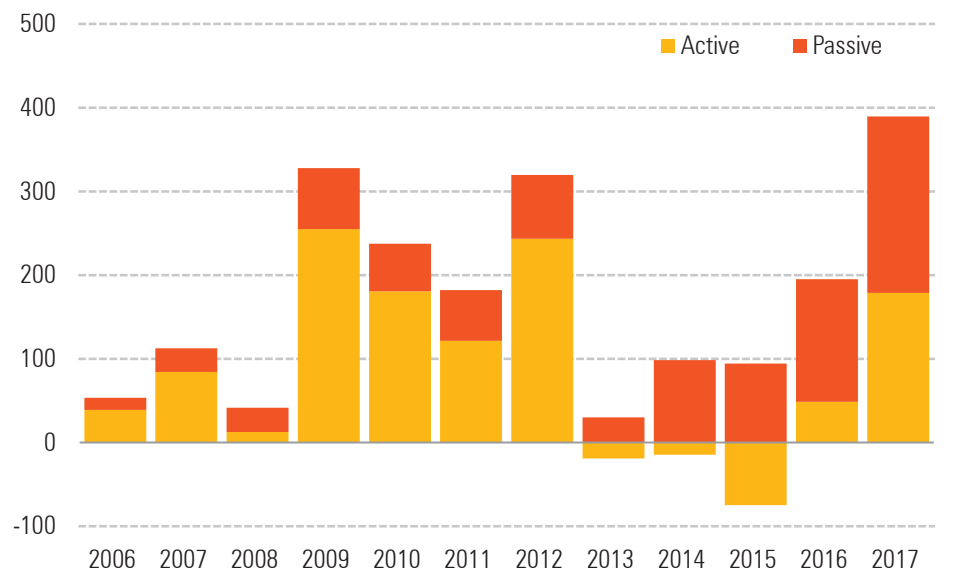
**Exhibit 6** U.S.-Equity Flows, Active Versus Passive (\$ Billion)



Source: Morningstar Direct Asset Flows.

- Active taxable-bond funds started to become popular again in the past two years.

**Exhibit 7** Taxable-Bond Flows, Active Versus Passive (\$ Billion)

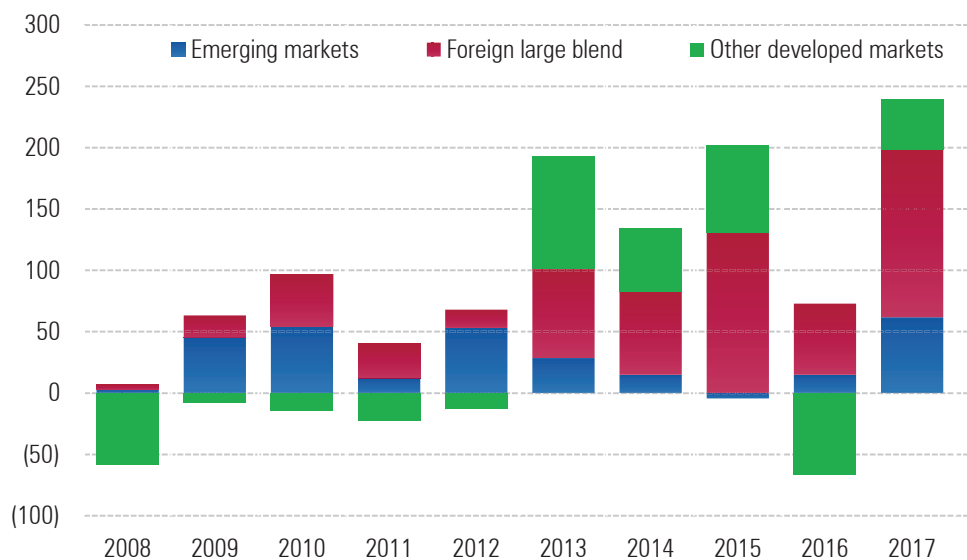


Source: Morningstar Direct Asset Flows.

	<b>2017 Return (%)</b>
S&P 500	21.8
MSCI EAFE	25.0
MSCI Emerging Markets	37.3

- After a drop in flows in 2016, investors once again started to diversify internationally, with a strong preference for foreign large-blend (which is mostly focused on Europe) in 2017.

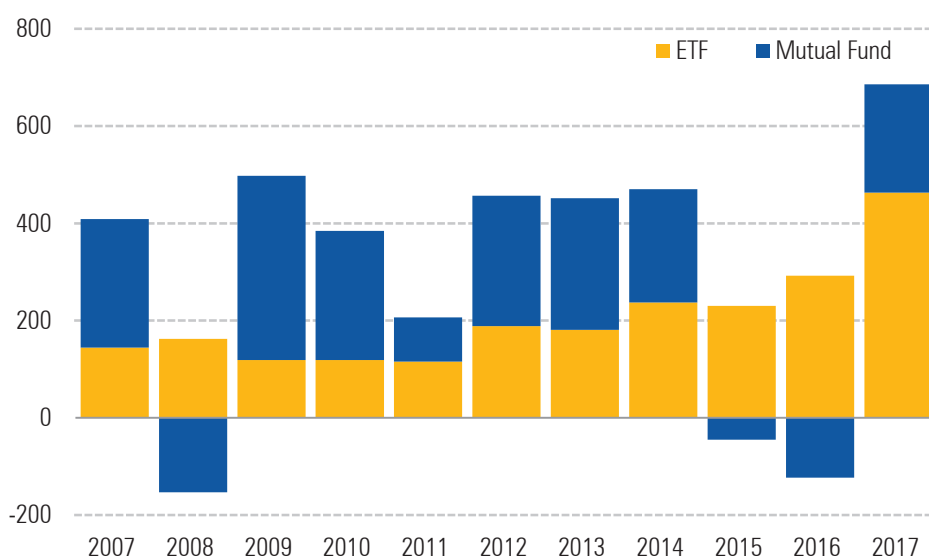
**Exhibit 8** Annual Flows to International Equity (\$ Billion)



Source: Morningstar Direct Asset Flows.

- Exchange-traded funds are becoming more and more popular.

**Exhibit 9** ETF and Open-End Fund Flows (\$ Billion)



Source: Morningstar Direct Asset Flows.

**Top- and Bottom-Flowing Morningstar Categories**

Estimated Net Flows* \$Mil	Active			Passive		
	Dec 2017	1 Year	Assets \$ Bil	Dec 2017	1 Year	Assets \$ Bil
<b>Leading</b>						
Intermediate-Term Bond	7,221	72,632	896	8,477	77,881	513
Foreign Large Blend	712	13,829	443	12,196	122,375	748
Large Blend	(3,912)	(38,099)	821	16,393	141,060	2,379
World Bond	490	2,296	140	3,324	30,224	104
Ultrashort Bond	1,292	30,741	133	1,596	9,319	20
<b>Lagging</b>						
Large Growth	(4,153)	(73,370)	1,351	(2,205)	17,193	258
High Yield Bond	(926)	(22,935)	263	(1,285)	4,135	47
Health	(839)	(9,674)	108	(1,006)	1,661	55
Muni National Short	(1,756)	4,343	123	(61)	520	6
Bank Loan	(1,093)	13,335	123	(286)	195	8

\*Excludes money market.

Source: Morningstar Direct Asset Flows.

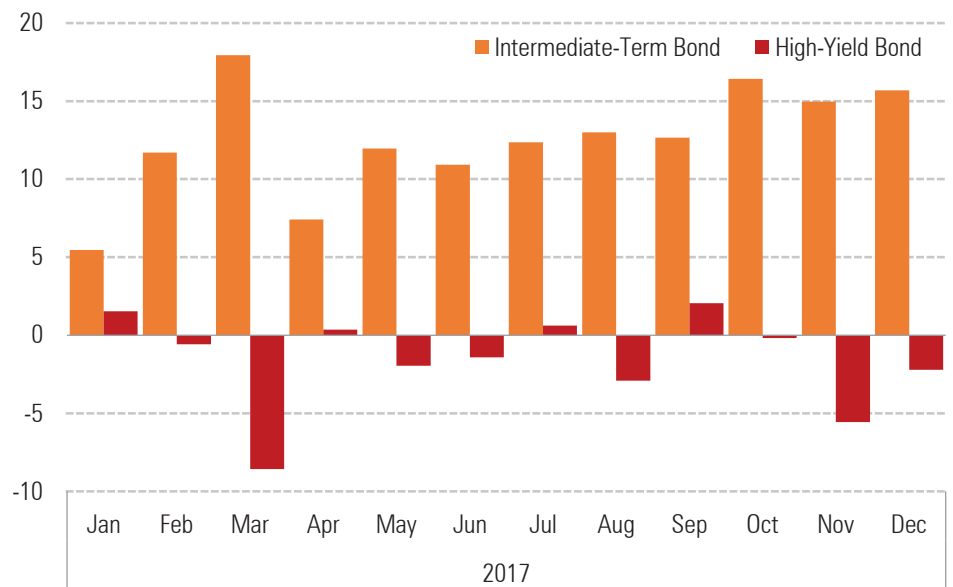
Intermediate-term bond and foreign large-blend were once again the two categories with the largest inflows in December. Large-blend (U.S.) landed third on the top-flowing list despite \$3.9 billion in outflows on the active side. Passive inflows were large enough (\$16.4 billion) to pull this category up in the ranks.

For the entire year, investors clearly preferred: 1) intermediate bonds, because they offer a good risk/return trade-off among fixed-income investments; 2) foreign large-blend, meaning diversifying equity allocations internationally (especially in Europe); and 3) large-blend, indicating investors haven't lost interest in the U.S. stock market at all. They just lost interest in overpriced and underperforming U.S.-equity funds.

Large growth suffered the largest outflows of all categories, with PowerShares QQQ, T. Rowe Price Growth Stock PRGFX, and American Funds Growth Fund of America AGTHX sustaining the worst redemptions.

High-yield bond came in second on the largest-outflows list in December, after making an appearance in the top position the previous month. The Tax Cuts and Jobs Act being signed into law may have had something to do with the outflows, because it is limiting the tax-deductible amount of interest expenses. High-yield debt companies will be negatively affected by this new provision because their interest expenses are much higher, and not being able to write them off will adversely affect profitability.

**Exhibit 10** Intermediate-Term and High-Yield Bond Monthly Flows (\$ Billion)



Source: Morningstar Direct Asset Flows.



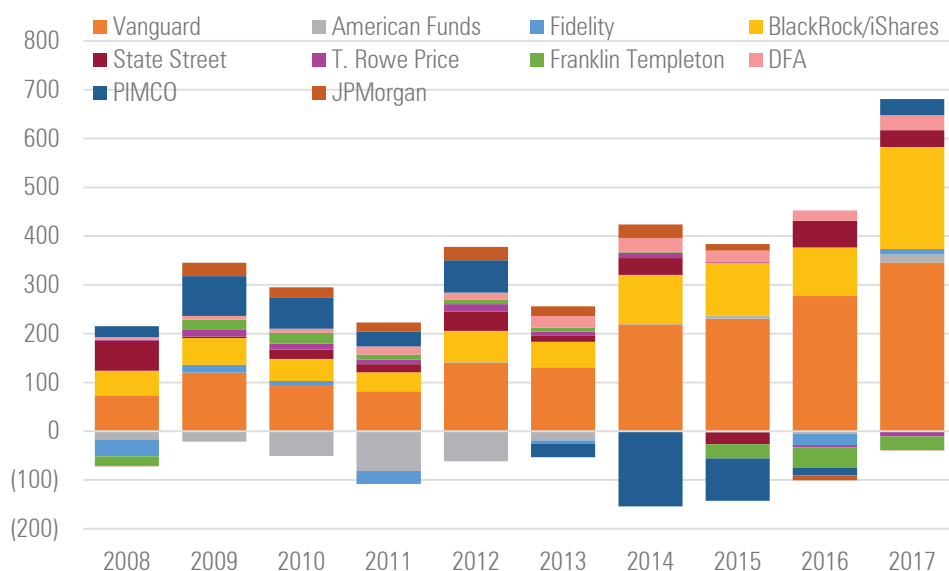
### Top 10 U.S. Fund Families by Assets Under Management

Estimated Net Flows \$Mil	Active			Passive		
	Dec 2017	1 Year	Assets \$ Bil	Dec 2017	1 Year	Assets \$ Bil
Vanguard	(627)	16,879	987	22,218	328,849	3,335
American Funds	(502)	16,629	1,524			
Fidelity Investments	(2,726)	(40,312)	1,108	6,360	51,288	363
BlackRock/iShares	8	(3,721)	217	9,022	213,278	1,382
SPDR State Street Global Advisors	(28)	1,918	7	18,174	32,000	616
T. Rowe Price	(1,031)	(5,617)	560	(1,068)	(5,244)	32
Dimensional Fund Advisors	1,689	31,157	403			
Franklin Templeton Investments	(2,920)	(28,155)	383	109	398	1
PIMCO	3,025	33,213	348	12	(200)	4
JPMorgan	1,306	(2,615)	296	1,240	2,100	9

Source: Morningstar Direct Asset Flows.

As the year drew to a close, State Street overtook T. Rowe Price to capture the fifth position among the top-10 largest fund families.

**Exhibit 11** Annual Flows into the Top-10 Fund Families (\$ Billion)



Source: Morningstar Direct Asset Flows.

PIMCO and DFA had the largest flows among active funds in December and for the entire past year, while Franklin Templeton and Fidelity continued to suffer outflows.

BlackRock/iShares was the runner-up on the passive side, still at a considerable distance behind Vanguard. The other two contenders, Fidelity and State Street, fell further behind, with much smaller inflows compared with the two leaders.

### Top-Flowing Active and Passive Funds

<b>Estimated Net Flows</b> \$Mil	<b>Dec</b> <b>2017</b>	<b>1 Year</b>	<b>Assets</b> <b>Dec</b> <b>2017</b> \$Mil	<b>Assets</b> <b>Dec</b> <b>2016</b> \$Mil
<b>Active Funds</b>				
PIMCO Income Fund	2,326	31,209	107,835	70,329
Vanguard Institutional Inter-Term Bd Fd	1,489	4,658	15,351	10,511
JHFunds2 Strategic Equity Allc Fund	1,046	374	7,707	6,962
Prudential Total Return Bond Fund	900	9,473	30,184	19,404
T. Rowe Price US Treasury Long-Term Fd	852	2,550	2,976	361
<b>Passive Funds</b>				
SPDR® S&P 500 ETF	12,062	3,951	277,542	224,820
Vanguard 500 Index Fund	4,292	45,129	391,435	282,566
Vanguard Total Bond Market II Index Fund	3,821	30,028	148,482	114,013
Vanguard Total Intl Stock Idx Fund	3,764	32,952	331,182	231,928
Vanguard Total International Bd Idx Fund	3,105	29,758	99,435	68,204

Source: Morningstar Direct Asset Flows.

PIMCO Income PIMIX was the clear flows winner in 2017 (despite a fee increase), with \$31.2 billion in new flows.

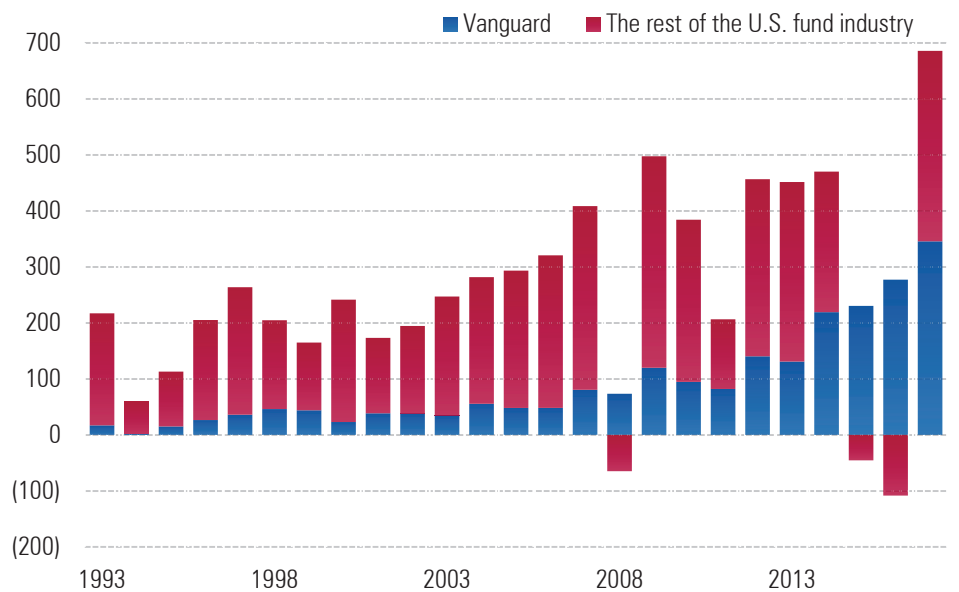
<b>Fund</b>	<b>Estimated Net Flow</b> <b>2017</b>
PIMCO Income Fund	31,208,822,237
Oakmark International Fund	9,660,584,242
Prudential Total Return Bond Fund	9,473,084,612
American Funds American Balanced Fund	7,851,476,343
Dodge & Cox Income Fund	5,800,966,691

Oakmark International OAKIX was the top beneficiary of the sustained international-equity flows last year, “partly because of excellent showings in 2016 and 2017. The strong team behind Oakmark International and its distinctive, repeatable process earn a Morningstar Analyst Rating of Gold,” writes senior analyst Greg Carlson, who covers the fund.

In the passive arena, SPDR S&P 500 ETF SPY received the largest flows in December, but this is a recurring trend each year as active managers rebalance their holdings and use this ETF to temporarily store cash.

Vanguard continued to dominate fund investing in 2017. However, there was a significant difference in flow patterns compared with previous years. In 2015 and 2016, Vanguard’s flows had been positive while the rest of the industry’s had been negative. In 2017, the flow numbers for both Vanguard and all the other providers, on aggregate, were in positive territory, signaling that some competitors are still able to give Vanguard a run for its money.

**Exhibit 12** Vanguard Versus the Rest of the U.S. Fund Industry (\$ Billion)



Source: Morningstar Direct Asset Flows.

**Bottom-Flowing Active and Passive Funds**

<b>Estimated Net Flows</b> \$Mil	<b>Dec</b> <b>2017</b>	<b>1 Year</b>	<b>Assets</b> <b>Dec</b> <b>2017</b> \$Mil	<b>Assets</b> <b>Dec</b> <b>2016</b> \$Mil
<b>Active Funds</b>				
Lord Abbett Short Duration Income Fund	(1,157)	3,646	41,179	37,030
Harbor International Fund	(1,136)	(10,425)	31,015	34,626
DoubleLine Total Return Bond Fund	(1,127)	(4,730)	52,877	55,703
T. Rowe Price Growth Stock Fund	(1,104)	(6,960)	51,658	44,642
American Funds Growth Fund of Amer	(1,034)	(5,350)	177,463	145,549
<b>Passive Funds</b>				
Vanguard Institutional Index Fund	(4,027)	(23,974)	232,158	211,496
iShares Russell 2000 ETF	(2,767)	137	43,293	38,364
PowerShares QQQ	(2,050)	2,060	58,262	41,793
iShares iBoxx \$ High Yield Corp Bd ETF	(1,926)	(1,382)	17,637	18,890
Industrial Select Sector SPDR® Fund	(1,204)	108	12,529	10,172

Source: Morningstar Direct Asset Flows.

Harbor International HAINX was the active fund with the largest outflows in 2017, owing to its “opportunistic misfires, middling results, and rising expenses,” in the words of senior analyst Kevin McDevitt. BlackRock Global Allocation MALOX landed second on the bottom-flowing list in terms of all-year flows, following heightened uncertainty after recent manager changes and process adjustments.

<b>Fund</b>	<b>Estimated Net Flow</b> <b>2017</b>
Harbor International Fund	(10,424,812,350)
BlackRock Global Allocation Fund	(7,430,363,867)
T. Rowe Price Growth Stock Fund	(6,959,940,549)
Fidelity® Series Value Discovery Fund	(6,721,341,318)
Fidelity® Low-Priced Stock Fund	(6,462,914,117)

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**Note:** The figures in this report were compiled on Jan. 10, 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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