

## NEWS RELEASE

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# Study Finds One-Third Drop in Total Cost of Stock Fund Ownership Since 1980, November 1998

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Washington, DC, November 16, 1998 - The total cost of investing in equity mutual funds has decreased by more than one-third between 1980 and 1997, according to a [new study](#) published by the Investment Company Institute, the national association of the American investment company industry.

"This is important research. We believe it will make a valuable contribution to the ongoing public discussion of mutual fund fees and expenses, particularly issues relating to the level and trend in the average cost of investing in mutual funds," Institute President Matthew P. Fink said. "Until now, the discussion has lacked a standard framework for analyzing the total cost of mutual fund investing. The Institute's study offers a comprehensive framework for analyzing mutual fund costs."

The study, [Trends in the Ownership Cost of Equity Mutual Funds](#), by the Institute's chief economist John Rea and senior economist Brian Reid, determined that the average cost of investing in equity funds decreased to 1.49 percent of each dollar invested in 1997 from 2.25 percent in 1980. "The cost of investing in mutual funds today is significantly lower than it was 18 years ago. At the same time, shareholders are receiving greater services and have more choice than ever before," Rea said.

The study also found evidence of economies of scale in equity funds. Large funds had substantially lower operating expenses than small funds. In addition, the 100 largest funds in 1997 that were established before 1980 experienced both rapid growth and falling operating expense ratios between 1980 and 1997. Among these 100 funds, those that grew most posted the largest reductions in operating expense ratios. "There is evidence of significant economies of scale at individual equity funds," Rea said. "It is important to remember, however, that by definition, economies of scale can be fairly examined only on a fund-by-fund basis not on an industrywide basis."

In addition, the study suggests that investors are sensitive to cost. "Although they have a wide range of cost ratios to choose from, investors clearly tend to concentrate their purchases among lower-cost equity funds," Rea said. He also noted that [previous Institute research](#) determined that an overwhelming majority of shareholders' equity fund accounts (77 percent) are in mutual funds that charge annual fees below the industry's simple average. Fink cited this research in [testimony](#) at a [Congressional hearing](#) in September.

Economists Rea and Reid evaluated fee trends using a measure called total shareholder cost. This measure represents the cost that an investor would expect to incur in purchasing and holding mutual fund shares. It accounts for all major fees, expenses, and sales charges relevant to decisionmaking, and is comparable to the fee information required by the U.S. Securities and Exchange Commission in every mutual fund prospectus.

The actual fees and expenses included in total shareholder cost consist of fund operating expenses, 12b-1 fees, and sales loads. In contrast, most other measures used to analyze mutual fund ownership cost do not incorporate all of these costs.

"Of the cost measures commonly used, most fail to account for the full range of mutual fund investment costs. As a result they misrepresent the actual cost incurred by the 'average' mutual fund investor. Total shareholder cost comes closest to capturing real investor cost," Rea said.

The decline in the total shareholder cost ratio between 1980 and 1997 was the result of lower distribution costs  $\frac{3}{4}$  the sum of annuitized sales loads and 12b-1 fees, Rea said. "Load funds substantially reduced distribution charges during the 18-year period," Rea said. "In addition, investors contributed to the decline by shifting fund purchases toward no-load funds."

The authors note that the downward trend in mutual fund ownership costs since 1980 is evident in other similar statistical measures. For instance, the asset-weighted average of total shareholder cost ratios declined nearly 40 percent, to 1.44 percent in 1997 from 2.31 percent in 1980. In addition, the simple average fell to 1.99 percent from 2.37 percent in the same period, while the median of the total cost ratio dropped to 1.96 percent from 2.88 percent.

"Taken together, all of these measures demonstrate that the cost of investing in equity mutual funds declined significantly between 1980 and 1997," Rea said

The Investment Company Institute is the national association of the investment company industry. Its members include mutual funds, closed-end funds, and unit investment trusts. The Institute's investor awareness publications include a brochure, [Frequently Asked Questions about Mutual Fund Fees](#).