CHAPTER 3

US Mutual Funds

A mutual fund is an investment company that pools money from shareholders and invests in a portfolio of securities. In 2024, 71.0 million US households owned mutual funds, representing more than 120 million individual investors. Investors rely on mutual funds to meet long-term personal financial objectives, such as education, a home purchase, or preparing for retirement. US households and institutions also use money market funds as cash management tools. Mutual funds, including money market funds, had net inflows of $127 billion in 2024, or 0.5 percent of year-end 2023 total net assets. Changing demographics, portfolio rebalancing, and investors' reactions to US and worldwide economic and financial conditions play important roles in determining how demand for specific types of mutual funds—and for mutual funds in general—evolves.

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Overview of Mutual Fund Trends

The US mutual fund industry remained the largest in the world, with $28.5 trillion in total net assets at year-end 2024. The majority of US mutual fund net assets were in long-term mutual funds, with equity funds alone making up 53 percent of US mutual fund net assets. Money market funds were the second-largest category, with 24 percent of net assets. Bond funds (18 percent) and hybrid funds (6 percent) held the remainder.

Investor Demand for US Mutual Funds

A variety of factors influence investor demand for mutual funds. For example, US households rely on equity, bond, and hybrid mutual funds to meet long-term personal financial objectives, such as preparing for retirement, saving for emergencies, or saving for education. US households, as well as businesses and other institutional investors, use money market funds as cash management tools because they provide a high degree of liquidity and access to short-term market yields.

Investor demand for mutual funds remained robust in 2024, as inflows into money market funds and bond funds more than offset outflows from equity funds and hybrid funds. Money market funds experienced strong demand as investors were attracted to high short-term yields. Bond mutual funds saw modest demand, with bond market returns and portfolio rebalancing likely playing key roles. By contrast, equity mutual funds experienced outflows in 2024 (despite strong stock market returns), primarily reflecting an ongoing shift to other products and portfolio rebalancing.

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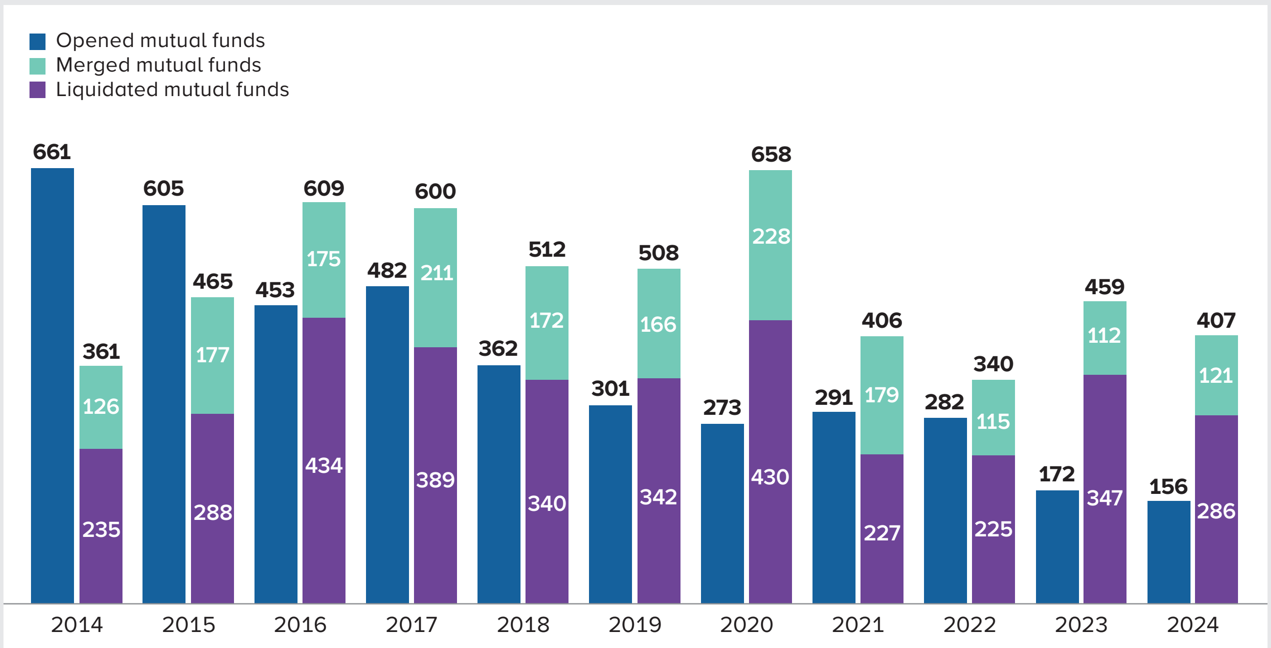
Entry and Exit of US Mutual Funds

Mutual fund sponsors create new funds to meet investor demand, and they merge or liquidate those that do not attract sufficient investor interest. A total of 156 mutual funds opened in 2024, down slightly from 2023 (Figure 3.1). A steep drop in the number of equity fund launches that was partially offset by an increase in bond fund launches contributed to the modest decline in the number of mutual funds that opened in 2024. During the same time, the number of mutual funds that were either merged or liquidated decreased 11 percent to 407 as sponsors eliminated fewer equity mutual funds from their lineups.

FIGURE 3.1

Mutual Funds Enter and Exit the Industry Because of Competition and Investor Demand



Note: Data include mutual funds that do not report statistical information to the Investment Company Institute and mutual funds that invest primarily in other mutual funds.

Investors in US Mutual Funds

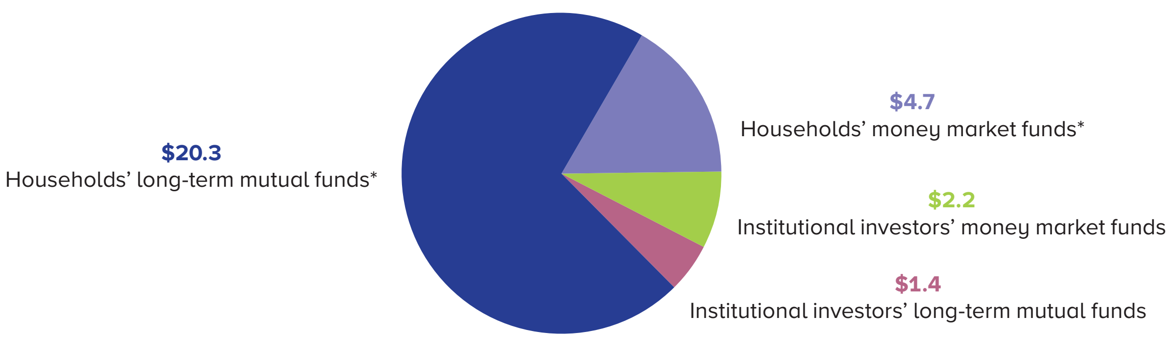
Demand for mutual funds is, in part, related to the types of investors who hold mutual fund shares. Retail investors (i.e., households) held the vast majority (88 percent) of the $28.5 trillion in US mutual fund net assets at year-end 2024 (Figure 3.2). When looking at only long-term mutual funds, the share of net assets held by retail investors was even higher (94 percent). Retail investors also held substantial money market fund net assets ($4.7 trillion), but this was a relatively small share (19 percent) of their total mutual fund net assets ($25.0 trillion).

By contrast, institutional investors such as nonfinancial businesses, financial institutions, and nonprofit organizations held a relatively small portion of mutual fund net assets. At year-end 2024, institutions held $3.6 trillion or 12 percent of mutual fund net assets (Figure 3.2), the majority (61 percent) of which was held in money market funds. One of the primary reasons institutions use money market funds is to help manage their cash balances.

FIGURE 3.2

Households Held 88 Percent of Mutual Fund Total Net Assets

Trillions of dollars, year-end 2024



Mutual fund total net assets: $28.5 trillion
Long-term mutual fund total net assets: $21.7 trillion
Money market fund total net assets: $6.9 trillion

* Mutual funds held as investments in individual retirement accounts, defined contribution retirement plans, variable annuities, 529 plans, and Coverdell education savings accounts are counted as household holdings of mutual funds.

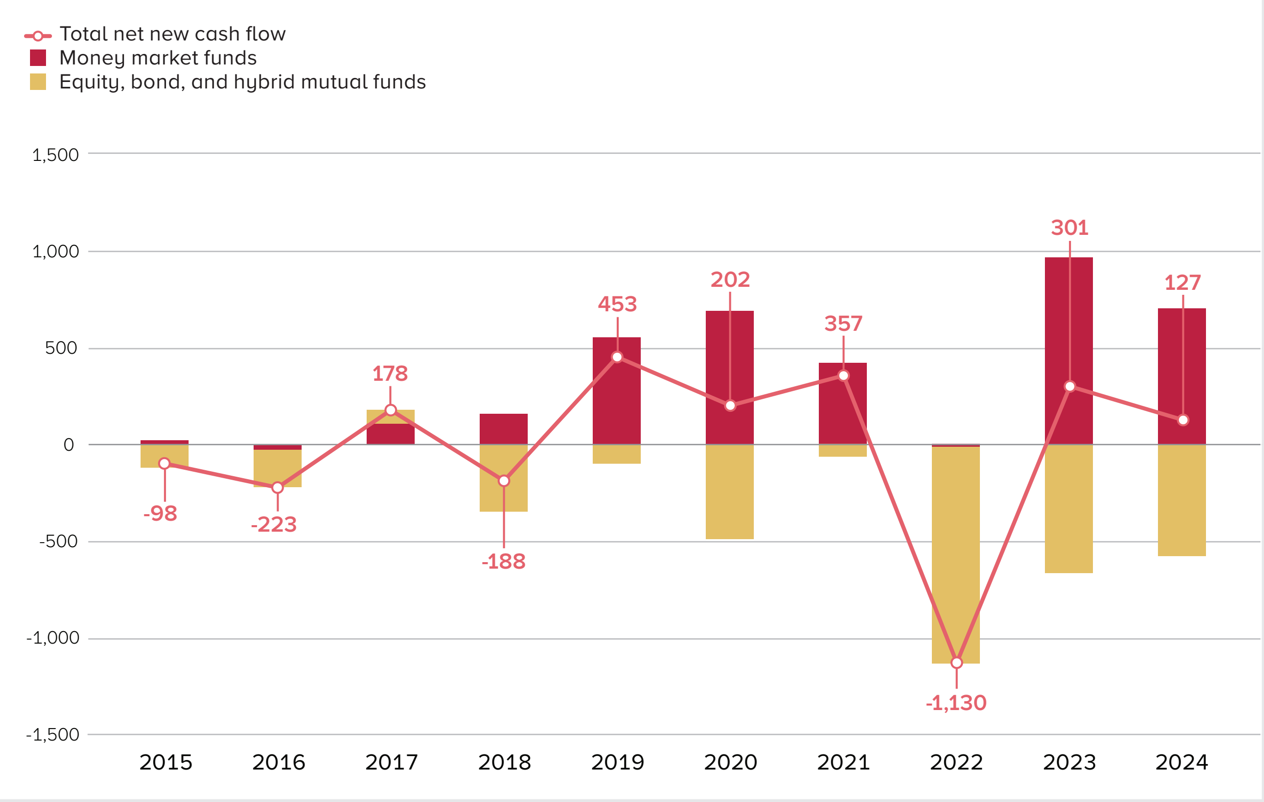
Developments in Mutual Fund Flows

Overall demand for mutual funds as measured by net new cash flow—new fund sales less redemptions, plus net exchanges—declined in 2024 (Figure 3.3). In 2024, mutual funds had net inflows of $127 billion (0.5 percent of year-end 2023 total net assets), following net inflows of $301 billion in 2023. Long-term mutual funds experienced net outflows of $576 billion in 2024, while money market funds saw net inflows of $703 billion. A number of factors—including interest rate risks, an evolving economic outlook, ongoing demographic trends, and demand for indexed products—appeared to influence US mutual fund flows in 2024.

FIGURE 3.3

Inflows to Money Market Funds More Than Offset Outflows from Long-Term Mutual Funds in 2024

Billions of dollars, annual



The US Economy and Financial Markets in 2024

The US economy and financial markets experienced a great year in 2024. The US economy grew at a solid pace of 2.8 percent, extending its exceptional performance relative to other major economies in recent years.* A healthy labor market, resilient consumer spending, and robust domestic investment all contributed to this economic growth. Although the unemployment rate ticked up from 3.8 percent in December 2023 to 4.2 percent in July 2024 and remained relatively stable in the second half of the year, this level was still low by historical standards. Inflation continued to ease in 2024. The year-over-year Consumer Price Index (CPI) growth declined from 3.4 percent in December 2023 to a three-year low of 2.4 percent in September 2024 before rebounding somewhat to 2.9 percent at year-end.

Convinced that tight monetary policy had produced sufficient progress on taming inflation and cooling economic activity, the Federal Reserve started to cut the federal funds rate, its benchmark interest rate, in September. By year-end 2024, the Federal Reserve had cut the federal funds rate by a total of one full percentage point to a target range of 4.25 to 4.50 percent.

Despite bouts of high volatility in 2024, US stocks had another strong year, with total returns of 23.8 percent, following total returns of 26.1 percent in 2023.† Strong corporate earnings, easing inflation, and the Federal Reserve's interest rate cuts fueled this equity market gain. Bonds performed well in the first three quarters of 2024 with a total return of 5.2 percent through September.‡ In the last quarter, however, bond markets reversed course, ending the year with a total return of 1.8 percent.

Long-Term Mutual Fund Flows

Although net new cash flows into long-term mutual funds are typically correlated with market returns, they tend to be a relatively small percentage of total net assets even during episodes of market turmoil. Several factors may contribute to this phenomenon. For example, households (i.e., retail investors) own the vast majority of US long-term mutual fund net assets (Figure 3.2). Retail investors generally respond less strongly to market events than do institutional investors. Most notably, households often use mutual funds to save for the long term, such as for college or retirement. Many of these investors make stable contributions through periodic payroll deductions, even during periods of market stress. In addition, many mutual fund shareholders seek the advice of financial advisers, who may provide a steadying influence during market downturns. Furthermore, because net assets in mutual funds are spread across more than 120 million investors who have a wide variety of individual characteristics (such as age or appetite for risk) and goals (such as saving for retirement, emergencies, or education), investors are also bound to have a wide range of views on market conditions and how best to respond to those conditions to meet their individual goals. As a result, even during months when funds as a whole experience net outflows, some investors continue to purchase fund shares.

* For example, in 2024, GDP growth was 1.0 percent in the European Union and 0.9 percent in the United Kingdom.

† As measured by the FT Wilshire 5000 Total Return Index.

‡ As measured by the S&P US Aggregate Bond Index.

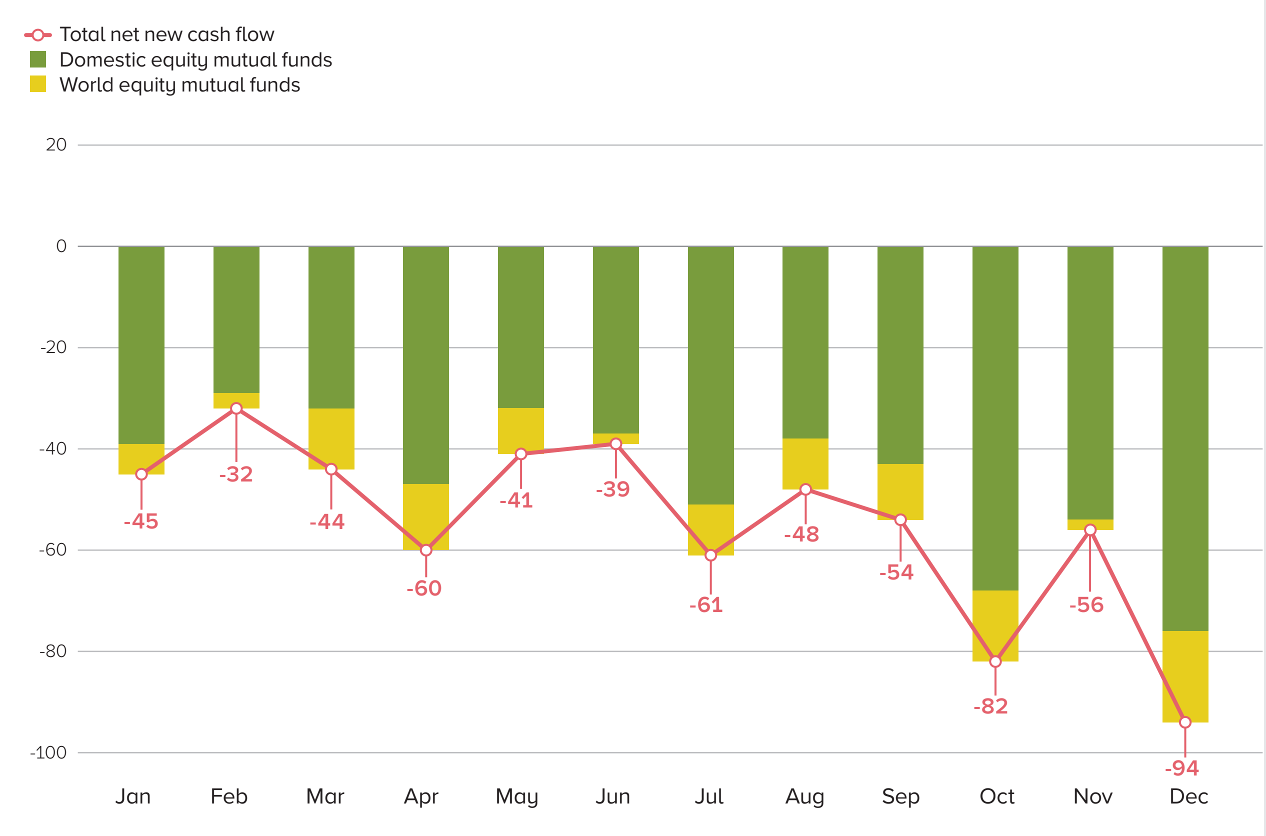
Equity Mutual Funds

Equity mutual funds experienced net outflows every month in 2024, totaling $655 billion over the year or 4.9 percent of their year-end 2023 total net assets (Figure 3.4). In the first three months of the year, investors had redeemed, on net, $120 billion from equity mutual funds. Flows to mutual funds, in general, tend to be bolstered in the first quarter of a year because investors who receive year-end bonuses may invest that money relatively quickly in the new year. In addition, some investors wait to make contributions to their individual retirement accounts (IRAs) before filing their tax returns. As the year progressed, net outflows from equity mutual funds accelerated, with investors redeeming, on net, $534 billion from April through December.

FIGURE 3.4

Equity Mutual Funds Experienced Net Outflows Throughout 2024

Billions of dollars; monthly, 2024



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Net outflows from equity mutual funds in 2024 were likely driven by continued investor demand for equity exchange-traded funds (ETFs) and portfolio rebalancing. As discussed in Chapter 4, demand for ETFs has been very strong for the past decade. Equity ETFs had net creations in every month of 2024, which resulted in $840 billion in net share issuance over the year (see Figure 4.4). By contrast, equity mutual funds had net outflows of $655 billion in 2024 (Figure 3.4). Additionally, portfolio rebalancing likely also played a role in outflows from equity mutual funds. As equity markets outperformed bond markets by a wide margin in 2024, investors and target date funds following asset allocation strategies would have needed to sell equity funds and buy bond funds to remain at their target allocations.

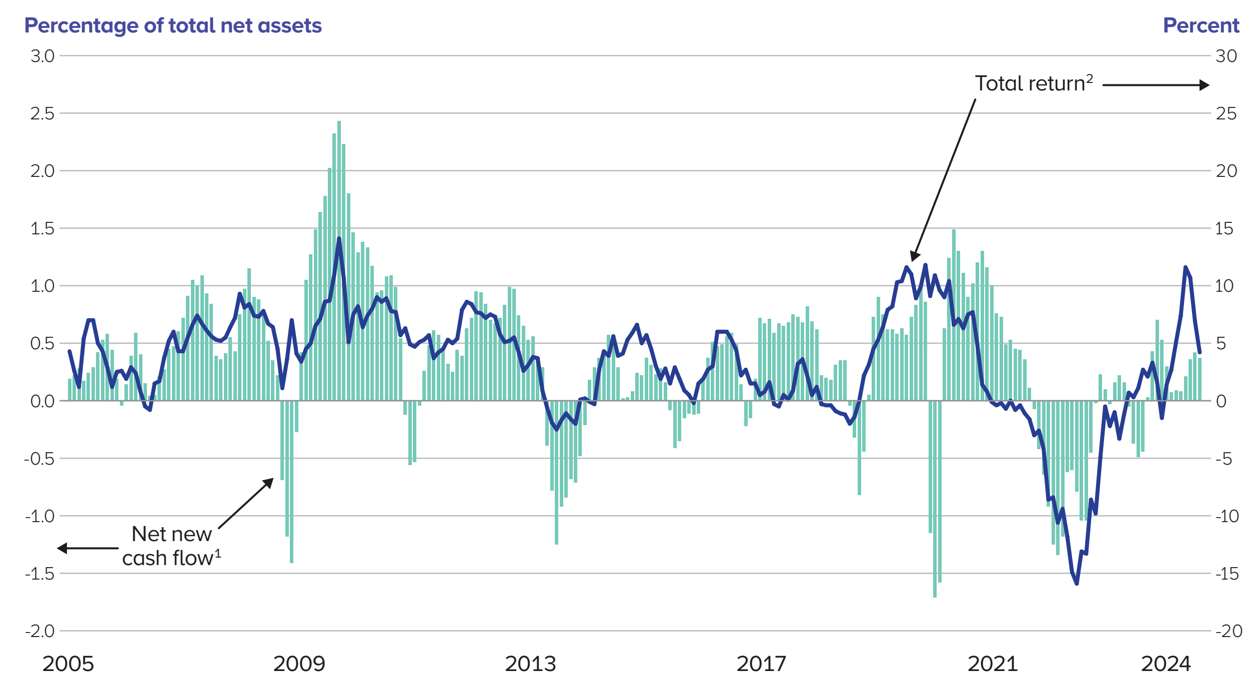
Bond Mutual Funds

Bond mutual fund net new cash flows typically are correlated with the performance of US bonds (Figure 3.5), which, in turn, is largely driven by the US interest rate environment. In 2024, bond mutual funds faced significant interest rate volatility, as long-term interest rates fluctuated widely throughout the year. The yield on the 10-year Treasury started 2024 at 3.9 percent, increased to 4.7 percent in late April, and then retreated to as low as 3.6 percent in September before bouncing back to 4.6 percent at year-end. A variety of factors, including inflation uncertainty, an evolving economic outlook, and shifting expectations of monetary policies, contributed to these fluctuations.

FIGURE 3.5

Net New Cash Flow to Bond Mutual Funds Is Typically Related to Bond Returns

Monthly



[1] Net new cash flow is reported as a percentage of previous month-end bond mutual fund total net assets, plotted as a three-month moving average. Data exclude high-yield bond mutual funds.

[2] The total return on bonds is measured as the year-over-year percent change in the FTSE US Broad Investment Grade Bond Index.

Sources: Investment Company Institute, FTSE Russell, and Refinitiv

Taxable bond mutual funds experienced net inflows of $163 billion in 2024, or 4.1 percent of their year-end 2023 total net assets (Figure 3.6), reversing two years of net outflows. In addition to the small, positive return on US bonds in 2024, portfolio rebalancing may have contributed to taxable bond mutual fund inflows as stocks significantly outperformed bonds in 2024.

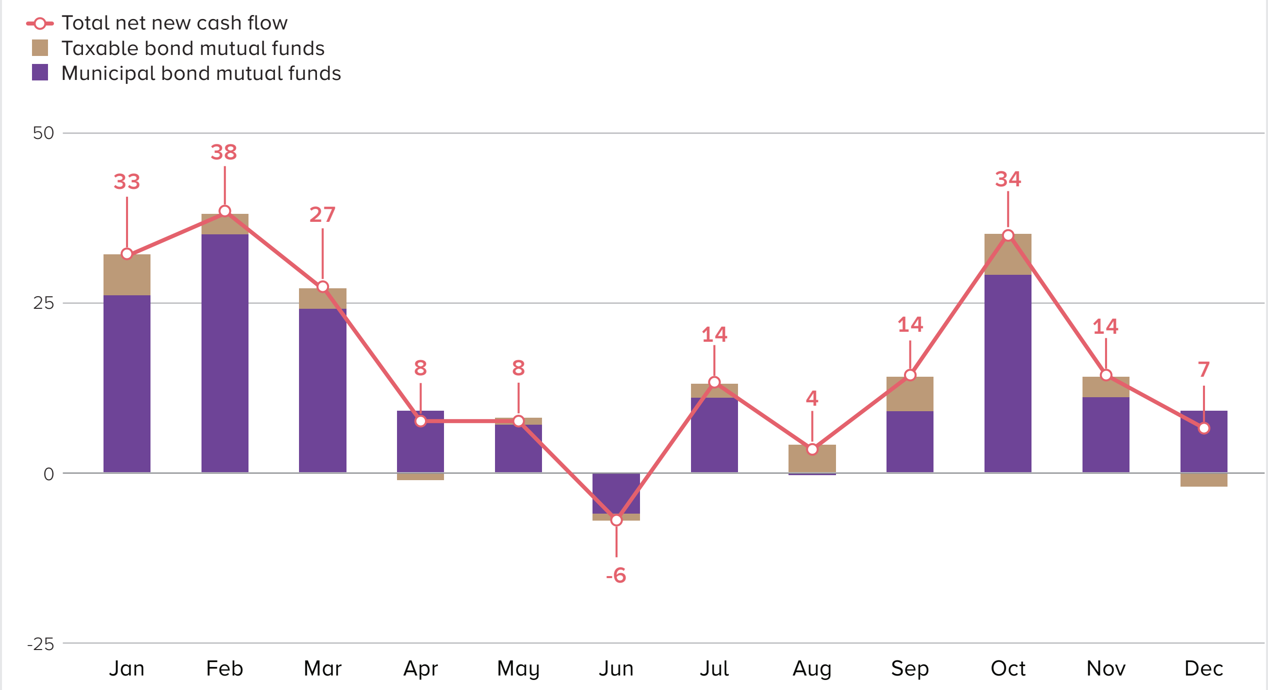
All categories of taxable bond mutual funds experienced inflows in 2024, with investment grade bond funds experiencing the bulk of inflows—$65 billion, which represented 2.9 percent of their year-end 2023 total net assets. Multisector bond mutual funds saw net inflows of $60 billion (10.8 percent); world bond mutual funds, which typically hold a mix of bonds denominated in US dollars and foreign currencies, saw net inflows of $28 billion (5.8 percent); high yield bond funds saw net inflows of $8 billion (2.5 percent); and government bond mutual funds saw net inflows of $2 billion (0.5 percent).

Municipal bond mutual funds also experienced inflows in 2024, with net inflows totaling $29 billion for the year, or 3.9 percent of their year-end 2023 net assets.

FIGURE 3.6

Net New Cash Flow to Bond Mutual Funds Was Generally Positive Throughout 2024

Billions of dollars; monthly, 2024



How Bond Mutual Funds Manage Investor Flows

When meeting redemptions, fund managers' actions are guided by market conditions, expected investor flows, and other factors. A fund might decide to sell some of its holdings to raise the cash needed to fulfill redemptions. But its choice of which particular securities to sell may depend on market conditions. For example, during a market downturn, with liquidity at a premium, some fund managers might seek to add shareholder value by selling some of their funds' more-liquid bonds (which, being in high demand, are trading at a premium to fundamental value). Other fund managers may conclude that it is necessary and appropriate to sell a representative "slice" of their funds' entire portfolios.

Bond mutual fund managers have other ways of meeting redemption requests. For example, a fund might already have cash on hand. Alternatively, the fund may use the cash that bond mutual funds receive each day in the form of interest income from bonds held in the portfolio, proceeds from matured bonds, or new sales of fund shares.

In addition, bond funds often use derivatives or hold liquid assets other than cash. For example, a high-yield bond fund might hold some portion of its assets in equities because equities are very liquid and the return profiles of high-yield bonds and equities can be similar. Derivatives can be more liquid than their physical counterparts, and funds are required to segregate liquid assets to support their derivatives positions. As these positions are closed, this cash collateral provides a ready source of liquidity to meet redemptions. This is especially true for many of the funds commonly called liquid alternative funds, as these funds are explicitly designed to allow frequent investor trading and do so in large measure through the use of derivatives.

Long-Term Demand for Bond Mutual Funds

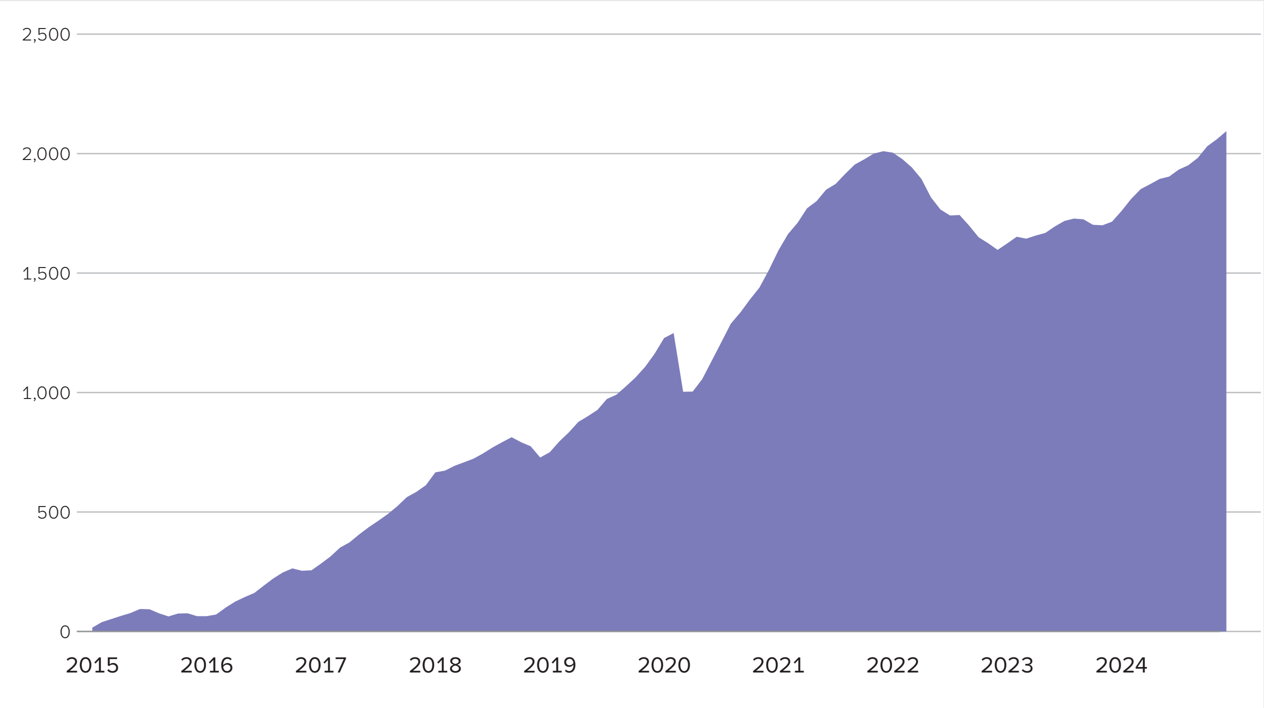
Despite outflows in 2022 and 2023, bond mutual funds have received $2.1 trillion in net new cash flows and reinvested dividends in the past decade (Figure 3.7).

A number of factors have contributed to this long-term demand for bond mutual funds, including demographics. Older investors tend to have larger account balances because they have had more time to accumulate savings and take advantage of compounding. At the same time, as investors age, they tend to shift toward fixed-income products. Over the past decade, the aging US population has boosted flows to bond funds.

FIGURE 3.7

Bond Mutual Funds Have Experienced Net Inflows Through Most of the Past Decade

Cumulative flows to bond mutual funds, billions of dollars, monthly



Note: Bond mutual fund data include net new cash flow and reinvested dividends.

The popularity of target date mutual funds has also contributed to strong demand for bond mutual funds during this period. Target date funds invest in a changing mix of equities and fixed-income investments. As the fund approaches and passes its target date (which is usually specified in the fund's name), the fund gradually reallocates assets from equities to fixed-income investments, including bonds. Over the past 10 years, target date mutual funds have received net inflows of $310 billion. At year-end 2024, target date mutual funds had total net assets of $2.0 trillion. Investor interest in these funds likely reflects their automatic rebalancing features as well as their inclusion as an investment option in many defined contribution (DC) plans (see Figure 8.10).

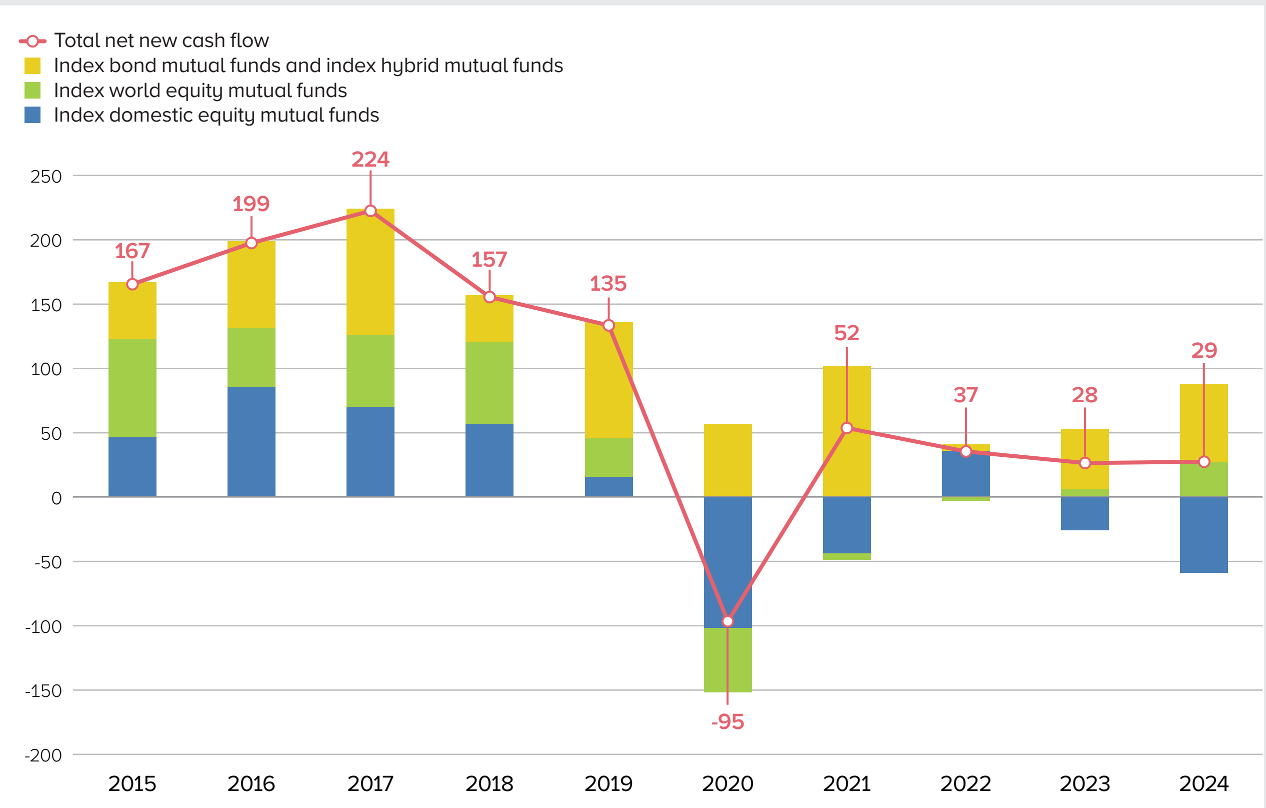
These long-term factors, combined with mostly positive annual returns on bonds and inflows from portfolio allocation strategies, have boosted bond mutual fund total net assets from $3.5 trillion at year-end 2014 to $5.1 trillion at year-end 2024. Even with this growth, long-term mutual funds' share of US bond markets—most of which is held by bond mutual funds—has stayed relatively stable in recent years (see Figure 2.4).

Growth of Other Investment Products

Outflows from some long-term mutual funds over the past decade reflect a broader shift, driven by both investors and retirement plan sponsors, toward other pooled investment vehicles. This trend is reflected in the outflows from actively managed mutual funds and the growth of index mutual funds, ETFs, and collective investment trusts (CITs) since 2007.

Index mutual funds—which hold all (or a representative sample) of the securities in a specified index—are popular among investors. Of households that owned mutual funds, 48 percent owned at least one index equity mutual fund in 2024. As of year-end 2024, 513 index mutual funds managed total net assets of $6.9 trillion. For 2024 as a whole, investors added $29 billion in net new cash flow to these funds (Figure 3.8). Outflows from index domestic equity mutual funds ($59 billion) were more than offset by inflows into index bond mutual funds and index world equity mutual funds ($62 billion and $27 billion, respectively).

FIGURE 3.8
Index Mutual Funds Saw Net Inflows in 2024
Billions of dollars, annual

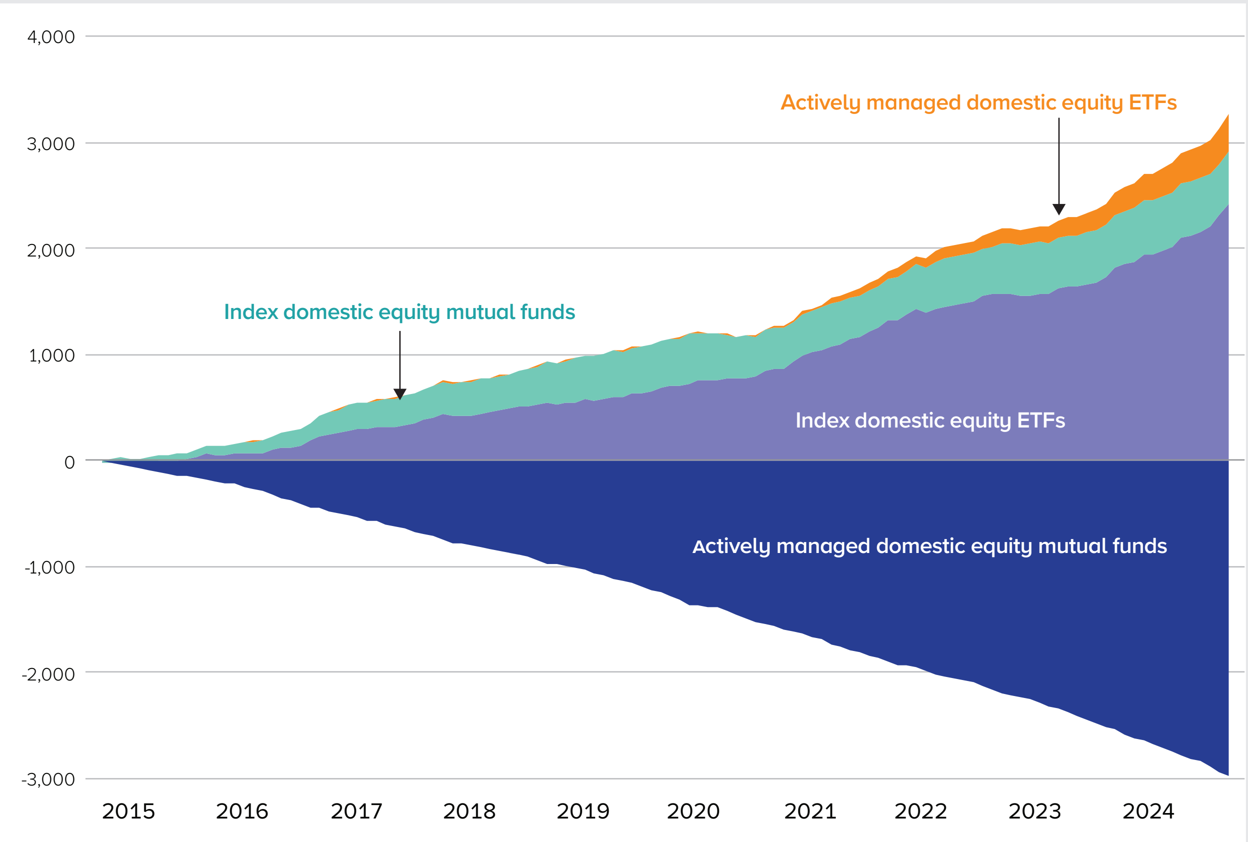


Index domestic equity mutual funds and ETFs have particularly benefited from the overall increase in investor demand for index-based investment products. From 2015 through 2024, index domestic equity mutual funds and ETFs received $2.9 trillion in net new cash and reinvested dividends, while actively managed domestic equity mutual funds experienced net outflows of $3.0 trillion (Figure 3.9). Index domestic equity ETFs have grown rapidly, attracting nearly five times the amount of net inflows into index domestic equity mutual funds since 2015. Part of the increasing popularity of ETFs in the past decade is attributable to more brokers and financial advisers using them in their clients' portfolios. In 2023, full-service brokers and fee-based advisers had 31 percent and 45 percent, respectively, of their clients' household assets invested in ETFs, up sharply from 9 percent and 18 percent in 2013 (Figure 3.10).

FIGURE 3.9

Some of the Outflows from Domestic Equity Mutual Funds Have Gone to ETFs

Cumulative flows to domestic equity mutual funds and net share issuance of domestic equity ETFs, billions of dollars, monthly

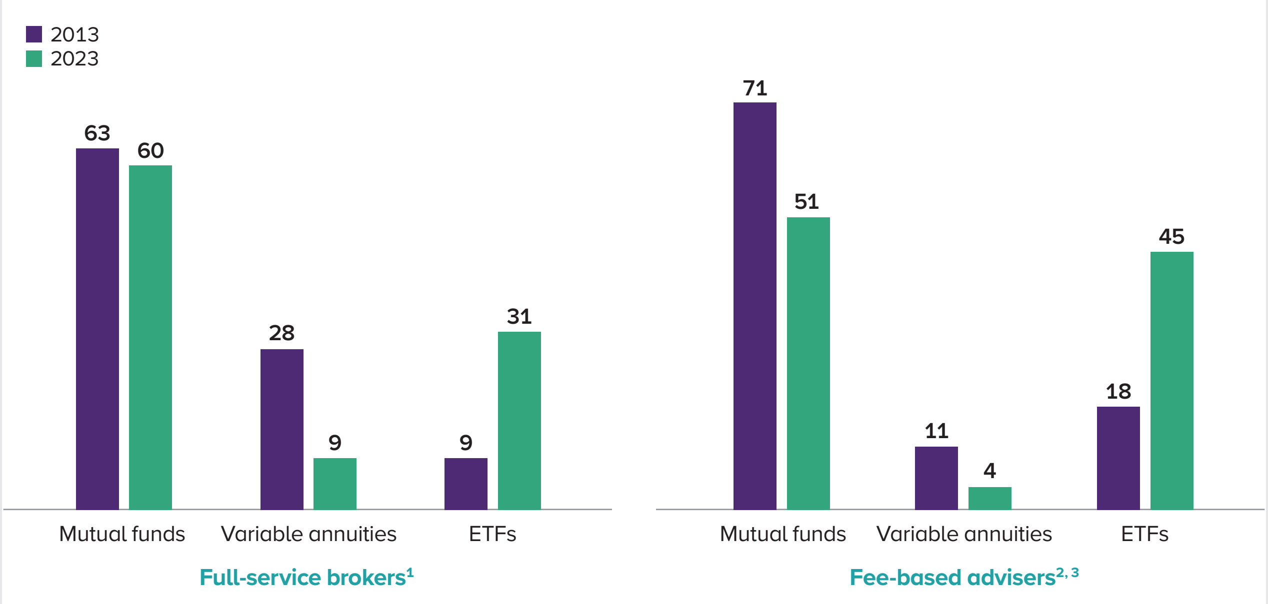


Note: Mutual fund data include net new cash flow and reinvested dividends; ETF data for net share issuance include reinvested dividends.

FIGURE 3.10

Fee-Based Advisers Are Investing Larger Portions of Client Portfolios in ETFs

Percentage of household assets invested in investment category by adviser type



[1] This category includes wirehouses as well as regional, independent, and bank broker-dealers.

[2] This category includes registered investment advisers and dually registered investment adviser broker-dealers.

[3] This category excludes an unknown portion of assets from investors who received fee-based advice but implemented trades themselves through discount brokers and fund supermarkets.

Note: In this figure, household assets include household holdings of mutual funds, variable annuities, and ETFs.

Source: Cerulli Associates, "The State of US Retail and Institutional Asset Management, 2024"

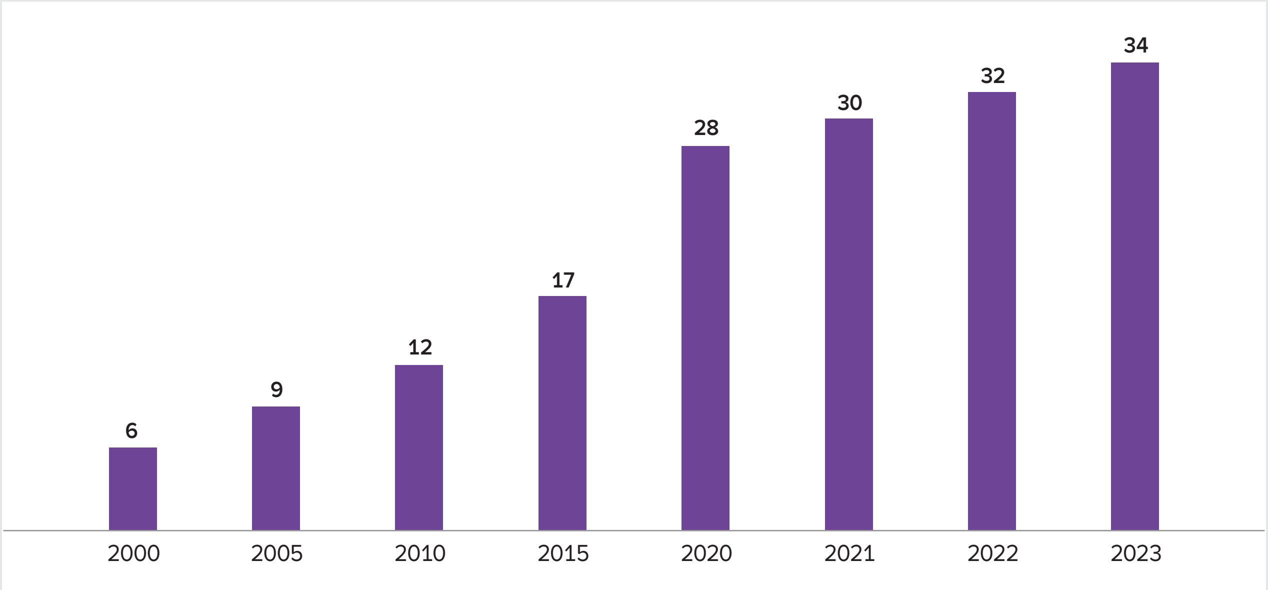
CITs are an alternative to mutual funds for DC plans. Like mutual funds, CITs pool the assets of investors and (either actively or passively) invest those assets according to a particular strategy. Much like institutional share classes of mutual funds, CITs generally require substantial minimum investment thresholds, which can limit the costs of managing pooled investment products. Unlike mutual funds, which are regulated under the Investment Company Act of 1940, CITs are regulated under banking laws and are not marketed as widely as mutual funds; this can also reduce their operational and compliance costs as compared with mutual funds.

More retirement plan sponsors have begun offering CITs as options in 401(k) plan lineups. As Figure 3.11 demonstrates, this trend has translated into a growing share of assets held in CITs by large 401(k) plans. That share increased from 6 percent in 2000 to an estimated 34 percent in 2023. This recent expansion is due, in part, to the growth in target date CITs.

FIGURE **3.11**

Assets of Large 401(k) Plans Are Increasingly Held in Collective Investment Trusts

Percentage of assets in large 401(k) plans*



* Large 401(k) plans are those that filed Form 5500 Schedule H (typically plans with 100 participants or more).

Note: Assets exclude Direct Filing Entity assets that are reinvested in collective investment trusts. Data prior to 2023 come from the Form 5500 Research data sets released by the Department of Labor. Data for 2023 are preliminary, based on Department of Labor Form 5500 latest data sets.

Source: Investment Company Institute calculations of Department of Labor Form 5500 data

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www.ici.org/viewpoints/25-view-mmf-reforms

Money Market Funds

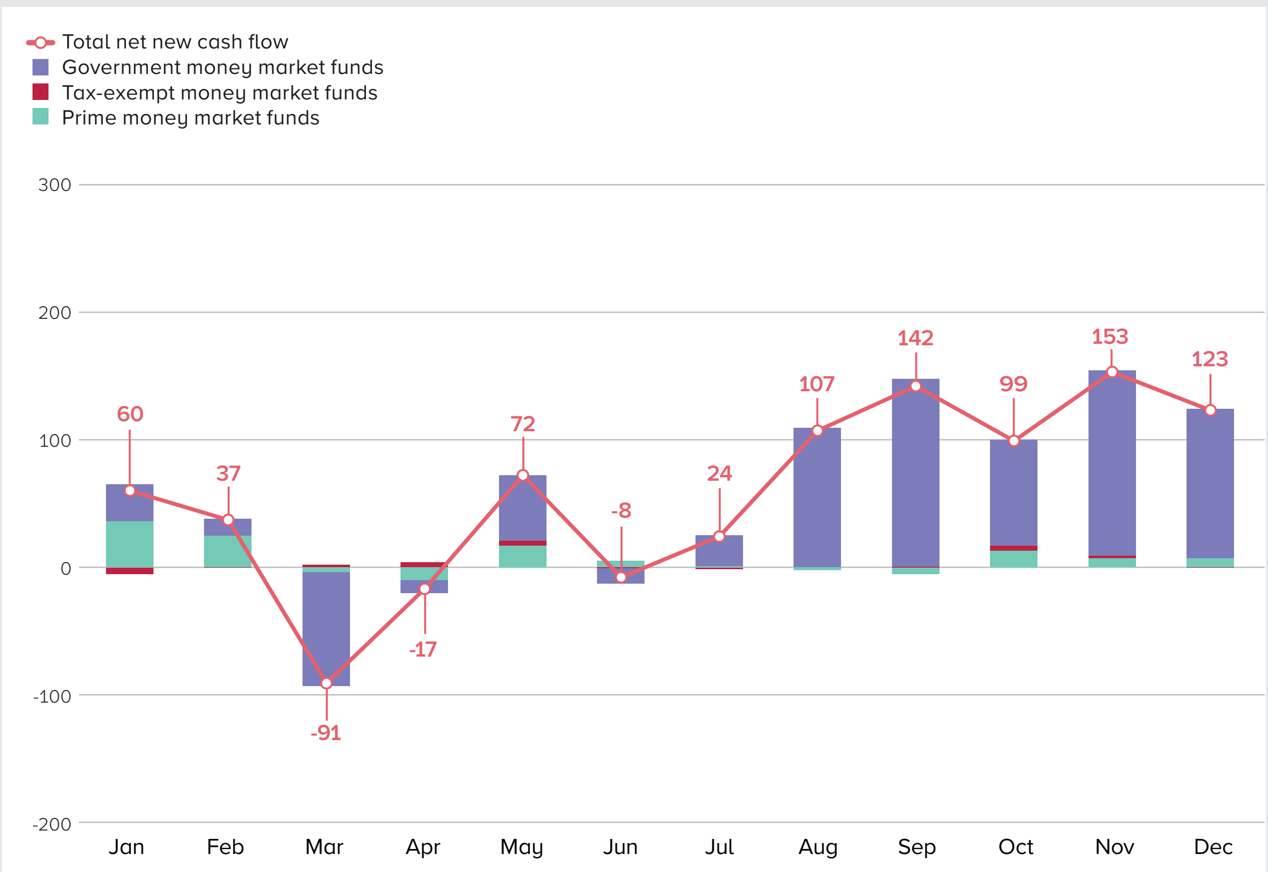
In 2024, money market funds saw substantial inflows of $703 billion (Figure 3.12) as short-term interest rates remained elevated. Demand was positive for all categories of money market funds in 2024, with government money market funds experiencing the bulk of inflows ($606 billion). Prime money market funds and tax-exempt money market funds saw inflows of $88 billion and $9 billion, respectively.

In July 2023, the Securities and Exchange Commission (SEC) adopted in its money market funds reforms a mandatory liquidity fee requirement for institutional prime money market funds. This new rule requires institutional prime funds to charge investors a liquidity fee under certain conditions, which is complex and costly for some money market fund sponsors to calculate. These concerns led 16 institutional prime funds to either liquidate or convert to government money market funds before the rule's implementation on October 2, 2024.* These funds had about $60 billion in net assets at the time of their liquidation or conversion.

FIGURE 3.12

Money Market Funds Experienced Strong Demand in 2024

Billions of dollars; monthly, 2024



* These data only include public institutional prime money market funds. Five nonpublic institutional prime money market funds, with about $220 billion in net assets, either moved to government strategies or liquidated or converted to non–money market strategies.