Wealth

Top Stock Pickers Crush S&P While Failing to Stem Outflows

By Michael McDonald and Annie Massa

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- U.S. active equity mutual fund outflows are at record pace
- Fidelity Contrafund returned 32% this year amid redemptions

In this article

SPX
S&P 500
3,824.68 USD
▲ +20.89 +0.55%

1768393D
AMERICAN FUNDS
Private Company

1618922Z
DIMENSIONAL FUND ADVISORS LT
Private Company

STT
STATE ST CORP
77.13 USD
▼ -0.60 -0.77%

BR
BROADRIDGE FINL
156.21 USD
▲ +0.59 +0.38%


Will Danoff *Photographer: Scott Eells/Bloomberg*

Star mutual fund managers are beating the soaring stock market in 2020 -- but customers are abandoning them for index-trackers anyway.

Will Danoff's $134 billion Fidelity Contrafund returned 32% this year through Wednesday, nearly 15 percentage points better than the S&P 500, yet investors yanked a net $23.4 billion, according to Bloomberg estimates. American Funds' $255 billion Growth Fund of America jumped 37% but lost more than $10 billion to net outflows. Their struggles have been replicated across an industry that's in danger of being overthrown by low-cost alternatives.

After decades as the dominant savings vehicle for long-term investors, U.S. actively managed stock mutual funds are heading for their worst ever year of outflows: around $500 billion, according to Bloomberg Intelligence estimates. By contrast, more than $200 billion has poured into equity exchange-traded funds, whose passive investing approach and tax-efficient structure have put them on course to permanently supplant human decision makers. If even the best managers can't lure new money, there's scant hope for everyone else.

“It’s like a freight train,” said Russel Kinnel, director of manager research at Morningstar Inc. “People got religion on fees and the big passive funds in general have delivered better returns because they’re cheaper.”

Active Exodus

These funds have beaten their benchmarks in 2020 but suffered outflows

Source: Bloomberg
* Fund closed to new investors. Note: All data as of Dec. 29

Companies that manage active funds say the data isn’t as dire as it may seem. They note that a growing number of investors have moved away from mutual funds to separately managed accounts with similar strategies at the same firm, even with the same portfolio manager.

Capital Group, which runs the American Funds lineup, saw higher redemptions during the early months of the Covid-19 pandemic. But its assets are up 12% this year to $2.2 trillion and its outflows are far below the industry average, a spokeswoman said, calling that “a testament to our focus to help investors grow their wealth over the long term.”

Fidelity Investments declined to comment on fund flows but stands by its broad lineup of active products.

“The mutual fund structure still has a great place in portfolios,” Tim Cohen, Fidelity’s co-head of equity, said in an interview.

Mutual fund companies that rely on stock picking benefited in recent years from an historic bull market that inflated assets even as investors peeled away, and there's no guarantee that run can continue. Market volatility and falling fees intensified pressure on fund companies to consolidate this year, with Morgan Stanley agreeing to buy Eaton Vance Corp. and State Street Corp. exploring potential mergers for its asset-management arm.

Read more: State Street Said to Weigh Options for Asset-Management Arm

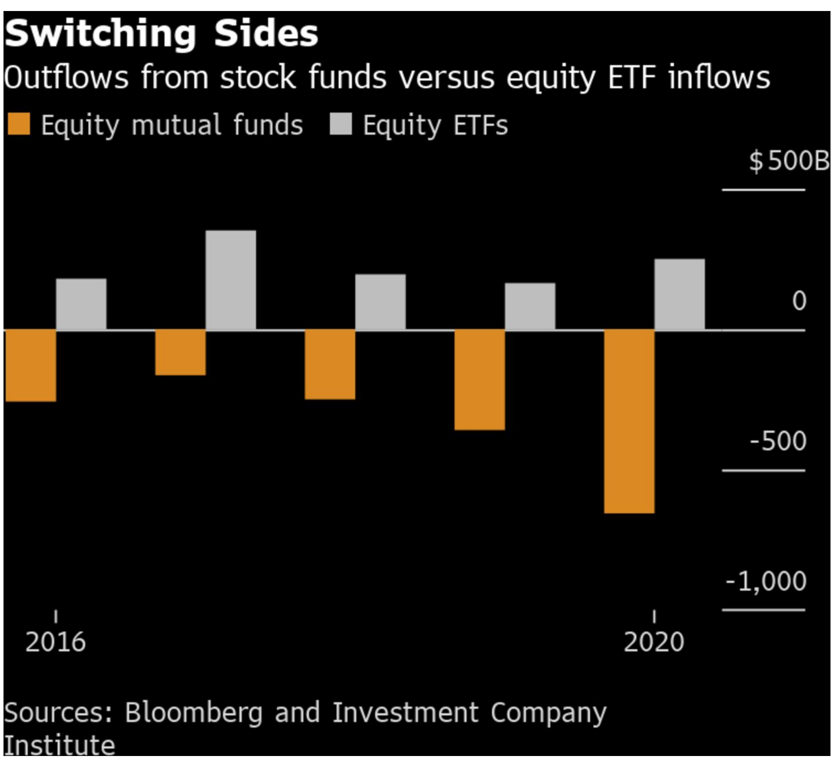
"In the past, performance was all that mattered," said Kyle Sanders, an analyst at Edward Jones. "Performance is important, but cost is becoming more and more important."

Financial advisers are helping to speed the move from active management, with 73% saying in a survey earlier this year by Broadridge Financial Solutions Inc. that they planned to keep increasing their ETF allocations.

One consolation for fund companies is that net deposits into actively run fixed-income products partly offset this year's outflows on the equity side. Some of the shift from stock funds can be attributed to rebalancing after the run-up, according to Sean Collins, chief economist at the Investment Company Institute.

Still, the industry is adjusting to the continued ascent of indexing. Quant giant Dimensional Fund Advisors is converting six of its funds, with about $20 billion, to ETFs. Fidelity is creating ETFs that mimic the performance of mutual funds including Blue Chip Growth and Magellan.

Changing tastes can affect revenue at companies such as Fidelity, which charges 85 cents per $100 invested in Contrafund. Passive exposure to the S&P 500 through an ETF can cost as little as 3 cents per $100.



Note: equity mutual funds include active and passive strategies. 2020 data through Dec. 25 Bloomberg

But those who pay up for Contrafund have been rewarded with annualized returns of 18% over the past five years, compared with the index's 15%. Danoff's fund isn't alone: at Capital Group's American Funds, the team-managed Growth Fund of America is also up an average of 18% since 2015.

Lesser-known funds with stellar returns are struggling to buck the outflows as well.

Artisan Partners in Milwaukee saw outflows from its Artisan Mid Cap Fund of about $765 million in 2020, according to Bloomberg estimates, despite surging 57%, making this one of the best years ever for the $7.3 billion fund. Over the past five years it's returned an annual average of 20%. Even with the fund's outflows, a spokesman said the firm's mid-cap strategy is "cash-flow positive" for the year when including separately managed accounts and trusts.

Matthew Kamm, who is part of the portfolio management team, said the investment firm has a large base of clients who have been loyal over the long term. Kamm, who joined Artisan in 2003, helps oversee more than $50 billion of assets across four stock-picking strategies.

"It's a relentless pressure on us, but it's not supposed to be easy," he said.

(Updates with returns through Wednesday in second paragraph.)