April Fund Flows: Investors Flock to Bonds

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Last Updated: May 16, 2024

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With the S&P 500 down in April, did investors continue to pile into equities or did higher bond yields drive flows there? We dive into the latest fund flows data for April to find out. Flows data measures the net movement of cash into and out of investment vehicles, such as mutual funds and exchange-traded funds (ETF). We typically analyze flows to gain insight on investor demand and sentiment surrounding different asset classes.

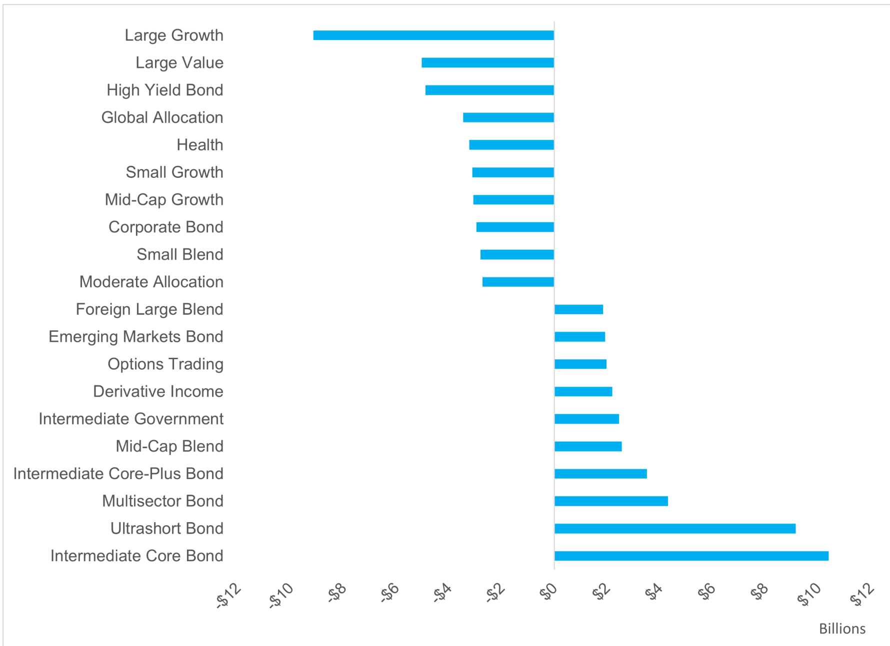
Investors Flock to Core Bonds and Dump Large Growth

When looking at flows by Morningstar category in April, investors treated core bond funds like an old comfortable recliner — a familiar place to kick back amid stock market turbulence — even the recliner itself is less than perfect (bonds were down in April as the yield on the 10-year Treasury rose by 27 basis points during the month). Intermediate core bonds experienced the largest inflow at over $10 billion, and multisector bonds gained over $4 billion as investors were attracted to fixed income by higher yields or were just avoiding equity markets. Ultrashort bonds also saw a large inflow, over $9 billion, from a cohort of investors who may be worried about interest rates heading higher still and wanted to minimize interest rate sensitivity. As yields increased throughout April (though they have come back down in May), the risk-reward trade-off of fixed income relative to equities appeared to become more tilted toward bonds, compelling investors to pile into bonds with five of the top six categories by inflows being fixed income related.

Looking at the other end of the spectrum, large growth equities saw the largest outflow in April at over $9 billion, as investors dumped this asset class during a month in which it fell by over 4% (the second-largest monthly decline since the start of 2023). Large value equities and high yield bonds also got hit by investors' risk-off appetite and saw large outflows.

Investors Rotate Into Core Bonds in April

1-Month Net Asset Flows (Top 10 and Bottom 10) Across Morningstar Categories (AUM, Billions $)

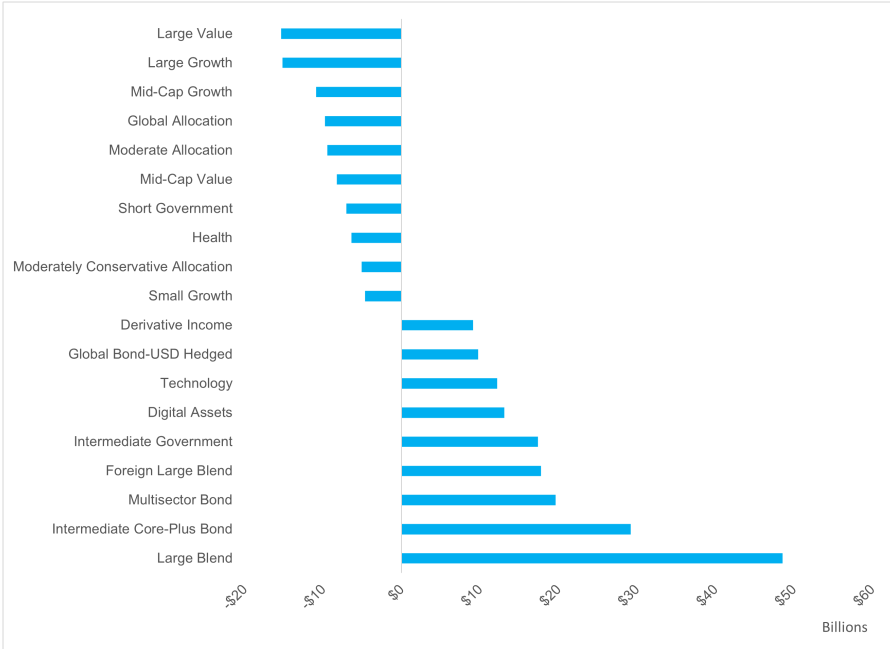


Source: LPL Research, Morningstar Direct 04/30/24
Disclosures: Indexes are unmanaged and cannot be invested in directly. Past performance is no guarantee of future results.

Large value and large growth equities are now experiencing the largest outflows year to date (YTD) with a more than $30 billion decline in assets between them; however, this is more than offset by an inflow of almost $49 billion into large blend equities. An explanation for this is the huge shift in the investing landscape currently occurring from (mostly active) large cap mutual funds to (mostly passive) ETFs, with ETF investors pouring into large blend faster than large growth or value. Large-cap mutual funds have seen combined outflows of almost $75 billion so far this year (large blend -$11 billion, large growth -$44 billion, and large value -$19 billion), but large cap ETFs have taken in $92 billion (large blend $60 billion, large growth $29 billion, and large value $4 billion). Digital assets also remain in the top 10 for inflows YTD despite seeing the first monthly outflow (-$115 million) for this newfound category of (mostly ETF) investments.

2024 Large Cap Flows Impacted by Shift from Mutual Funds to ETFs

YTD Net Asset Flows (Top 10 and Bottom 10) Across Morningstar Categories (AUM, Billions $)



Source: LPL Research, Morningstar Direct 04/30/24
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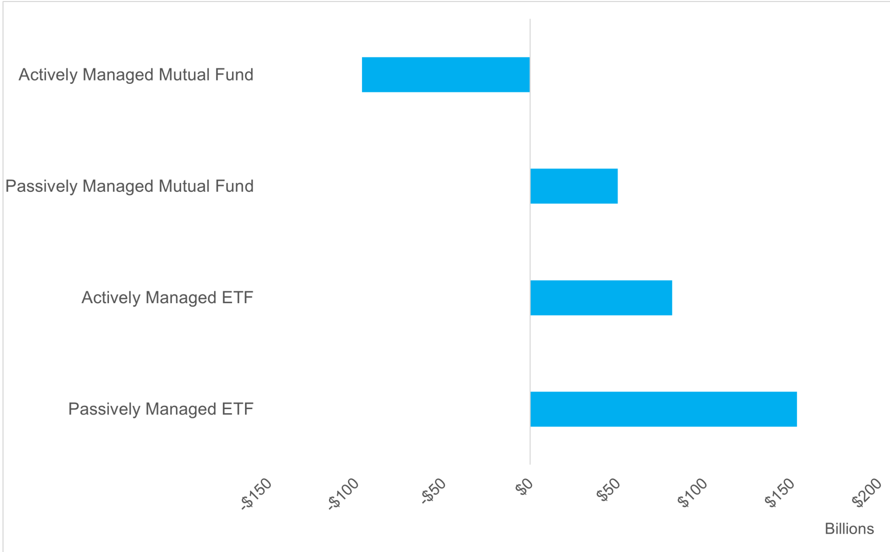
Are Active Mutual Fund Losses, Active ETF Gains?

Confirming the shifts occurring in investor vehicle choice is the YTD flows data broken out by investment and vehicle type. Overall, mutual funds have lost over $46 billion YTD, but that masks an even bigger flow out of active mutual funds (-$96 billion). Where has that money gone? ETFs have been the big winners with inflows of over $232 billion, just over a third of which has gone into the relatively new area of active ETFs. These relative trends, out of active mutual funds and into active ETFs, seem to be accelerating. In all of 2023, active mutual funds only lost just over $5 billion and active ETFs were only a quarter of total ETF inflows.

Active ETFs Boost ETF Inflows while Active Mutual Funds Shrink

YTD Net Asset Flows by Investment and Vehicle Type (AUM, Billions $)



Source: LPL Research, Morningstar Direct 04/30/24
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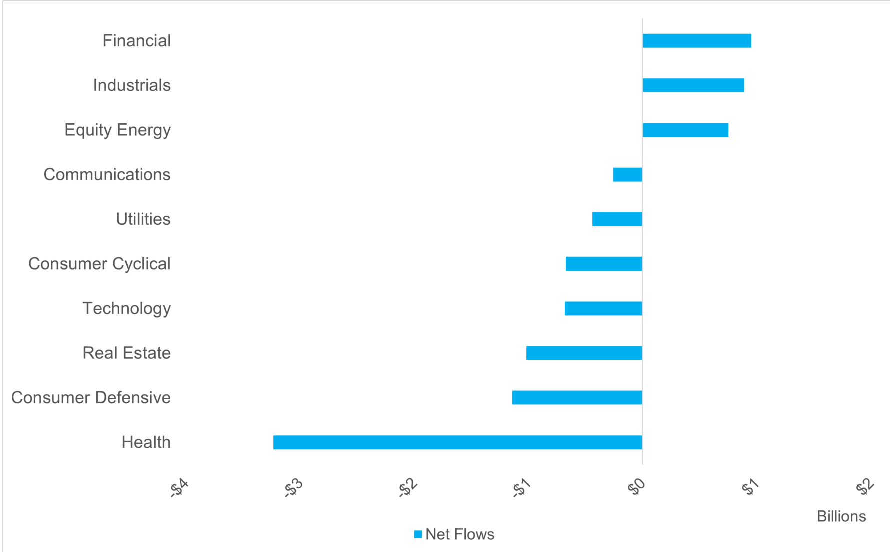
Investors Keen on Financials but Shun Health Care

Equity sector flow data in April showed the financial sector having the largest inflow, gaining just under $1 billion over the month. Industrials and energy rounded out the only other sectors to have net inflows. There appeared to be some element of performance chasing exhibited in these flows, with each of these sectors outperforming the wider S&P 500 coming into April.

Conversely, healthcare experienced the largest outflow in April at $3.2 billion, followed by consumer defensive and real estate. Healthcare was a laggard sector leading into April and continues to struggle with a slowdown in medical device sales, patent expirations, and a drop in COVID-19-related revenue. For contrarian investors, valuations in this sector appear attractive relative to history. Real estate outflows are no surprise given how much the sector has lagged — it is the only sector down YTD (-4%).

Financials Lead the Way in April Flows

1-Month Net Asset Flows across Morningstar Equity Sectors (AUM, $ Billions)



Source: LPL Research, Morningstar Direct 04/30/24
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Year-to-date, technology continues to dominate sector flows, with the sector adding over $12 billion. Given the run-up in the 'Magnificent Seven' stocks and, more broadly, U.S. growth equities, it's no surprise that technology is at the top of the list. Industrials is the only other sector with a significant net inflow (+$2 billion). Meanwhile, defensive sectors such as healthcare, utilities, and consumer defensives, have experienced the largest outflows, perhaps a reflection of the overall risk appetite of equity (sector) investors year to date.

Summary

We track flows data as it can expose more strategic market trends (like the shift to ETFs) as well as more tactical opportunities, such as indicating when assets coming into or out of an asset class have become extreme and might be poised to reverse.

When comparing the latest LPL Research Strategic and Tactical Asset Allocation Committee (STAAC) tactical views with the April flows data, bond funds had the largest inflows in April, which aligns with the STAAC's tactical stance that bonds have a slight edge over stocks currently when looking out to year-end. Even so, the improved economic and earnings outlook this year has kept the risk-reward trade-off for stocks and bonds well balanced. The STAAC maintains its neutral equities stance tactically, while also recommending a modest overweight to fixed income, funded from cash.

The Committee recommends a very modest tilt toward the growth style (which has seen the most outflows so far this year — some of which is due to the changes in the investment vehicles discussed above) after reducing its overweight position in mid-March. Higher-for-longer and steady economic growth favors value in the short term, but once the disinflationary trend resumes and rates calm down, as they have this week, look for growth to benefit from its superior earnings power. Communication services and energy remain favored sectors even though both have seen net outflows YTD.

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George Smith

George Smith chairs the Tactical Model Portfolio Committee, which manages LPL Financial's multi-asset models across multiple managed account platforms.