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Study Reveals Mutual Funds Have Done No Better Than Stock Market

Editor's Note: The operation of mutual funds recently was the subject of an exhaustive study. The following dispatch is an analysis of how effective they are in investing for their shareholders in the stock market.

By EDWARD COWAN
United Press International

Washington — (UPI) — A major study of the mutual fund industry comes to the conclusion that the funds as a group have done no better in the business of making money in the stock market than the market itself.

That is, the funds' performance about equaled that of the Standard and Poor's 500-stock average.

This comparison raises the provocative question of whether the average investor might not just as well play the market directly as indirectly by buying shares in a mutual fund. A mutual fund is an investment company whose business is buying securities, chiefly common stocks.

Examined Industry

Prof. Irwin Friend, head of a four-man team at the Wharton School of Finance, University of Pennsylvania, which examined the mutual fund industry, said the answer to the question is this:

If investors bought a random selection of stocks listed on the New York Stock Exchange, they would on the average do as well as a mutual fund. The word "average" in this case means the sum of losses by some of these investors and profits by others.

Which gets to why people buy mutual funds. They don't want to choose which stocks to buy. They feel they don't know enough about the market and they don't have the time or background to find out.

Moreover, they don't have enough money to diversify their investments for safety's sake — to buy a sufficiently broad variety of stocks so that they don't have all their money in one or two industries.

Sales Commission

What about the 8 per cent sales commission most mutual funds charge? Can't the direct investor avoid that.

For the small investor who can ill afford large risks, Friend said, achieving diversification comparable to that given by a mutual fund could cost more in brokerage fees than 8 per cent. There also are the costs and inconvenience of bookkeeping, he noted.

However, Friend observed that purchasers of "front end load" monthly investment plans may realize "only limited returns" if they drop the plan after one or two years. Because a sales commission figured over the life of the plan is deducted at the "front end," it may exceed 50 per cent of first-year payments and 30 per cent of payments in the first two years.

Most people with a few hundred or even several thousand dollars in a fund probably would conclude from the study that, all things considered, they might as well leave their money in. Not a few undoubtedly are satisfied if they do only as well as the market — at least on a rising market.

Grown Enormously

Since the first open-end investment company was formed in 1924, the mutual fund industry has grown enormously. After nearly being extinguished by the 1929 crash, the industry began to recover.

Its great days came in the bull market after World War II. As of Dec. 31, 1961 there were 344 open-end mutual funds with assets of $24.4 billion. An estimated 5.3 million individuals were share holders. Open-end means no limit to the amount of money the fund can take in and invest.

The Wharton school study of 189 funds, made for the Securities and Exchange commission, is the most exhaustive examination of the industry in more than 20 years. Although nominally analytical, it breaks out in several places with clearly implied criticism.

Probably its most pointed observation is that there are "potential conflicts of interest" in fund practices and in their affiliations with investment advisers and stock brokers.

Appear Higher

The discussion of "potential conflicts of interest" was based on the funds' managements profiting excessively at the expense of their shareholders. More specifically, advisory and brokerage costs appear higher than they need be, especially for the larger funds. Lower costs could be reflected in increashed dividends to shareholders.

The funds undoubtedly will have more to say about this. They already have said that fees paid advisers, based on fund size, are inadequate when a fund is young and small. Therefore, it would be unfair to scale fees down as they grow with a fund, even though the cost of advising the fund rises less rapidly than the fee.

Friend said his study team was making no ethical judgment about funds, although he did say they encourage economic growth by lowering the cost of capital. He declined to describe the 595-page report as either favorable or unfavorable to the industry.

Three Local Men To Attend Convention

Larry Rose, Walter L. Wilson, and Randy Hugdahl, members of the local branch of the National Association of Letter Carriers, will attend the 43rd biennial convention of the group. The convention will begin Sunday, Sept. 2, in Denver, Colo.

William C. Doherty, Cincinnati, will retire as president of the NALC this year. He has served 30 years as a national officer and 22 years as president.

Old Time Cars To Be in Jubilee Event

The Old Time Car club will participate in the Illinois Valley Labor Day Jubilee in Cave Junction Sept. 3. Members will meet at 10:15 a.m. and the parade will begin at 10:45 a.m.

Members should wear old timer costumes. Following the parade, cars will be exhibited at the rodeo grounds, the club members will visit the Kerbyville ghost town, and a picnic will be held at Selmac lake.

The club will meet at 3 p.m. Tuesday, Sept. 11, at the club house.