Strategic Insight
805 Third Avenue, New York, NY 10022
Tel: (212) 944-4455, Fax: (212) 730-7730
Available at **www.sionline.com**

WINDOWS

Into the

Mutual Fund Industry

February 2012

		Page
Perspectives 2012	**Perspectives**	**2**
US-Based Domestic Funds: 2011 Review	**US Fund FlowWatch**	**3**
US-Based International Funds: 2011 Update	**US Fund FlowWatch**	**6**
Global Trends: Growth Opportunities in Latin America	**Global Trends**	**7**
ETF Update: 2011 US ETF Flows Top $100B	**ETFs**	**9**
Record Flows into Income-Oriented US Stock Funds	**Product Development**	**11**
New Fund Launches: Big Debuts in 2011	**New Funds / Filings**	**13**
Closed-End Funds: The Market Evolves	**Closed-End Funds**	**14**
DC Plans: QDIA Opportunities	**Defined Contribution**	**15**
Alternative Fund Demand Among Discretionary FAs	**Distribution**	**16**
529 College Savings: Retooling the Advisor Channel in 2011	**529 Plans**	**18**
Innovation, Refocus on 2012 VA Agenda	**Variable Annuities**	**19**

© Copyright 2012 Strategic Insight, an Asset International Company, and when referenced or sourced Morningstar Inc. and Lipper Inc. All rights reserved. The information, data, analyses and opinions contained herein (a) include confidential and proprietary information of the aforementioned companies, (b) may not copied or redistributed for any purpose, (c) are provided solely for information purposes, and (d) are not warranted or represented to be correct, complete, accurate, or timely. Past performance is no guarantee of future results. The aforementioned companies are not affiliated with each other. Reproduction in whole or in part prohibited except by permission.

Any data or commentary in this report is for the internal use of client management companies only and is not to be disseminated to the general public and sales intermediaries in the form of regulatory or other reports, promotional material, or advertising without the prior written consent of Strategic Insight.

This report has been prepared using information and sources we believe to be reliable; however, we make no representation as to its accuracy, adequacy or completeness, nor do we assume responsibility for any errors or omissions or for any results obtained from the use of this report, including any action taken with respect to securities referred to in this report. Our employees may from time to time acquire, hold or sell a position in securities mentioned herein. We may from time to time perform services for any company mentioned in this report. This report is not a prospectus or representation intended to use in the purchase or sale of any securities mentioned in this report.

Strategic Insight is available by subscription and by single copy upon request to the publisher.

Perspectives 2012

Avi Nachmany
(212) 944 4451
avi@sionline.com

In this edition: US mutual fund 2011 trends; opportunities in Latin America; successful new open- and closed-end funds, as well as ETF innovations; "alt" funds used in BD discretionary accounts; an update on VAs; comments from SI's new FRC subsidiary on 529 plans; the record inflows to high-dividend stock funds, a theme to persist in 2012; and more.

Looking back: With slowing equity fund sales in 2H, industry new sales for all of 2011 rose just by 7% from their 2010 pace. Dollar redemptions, spiking in the summer, actually rose 16% for the full year. Thus, overall, net flows to long-term funds fell in 2011. **Yet about half of all managers – as well as half of all actively-managed bond and stock funds of size - still enjoyed positive flows last year.** Of the industry's aggregate $2.5 trillion **of new sales of stock and bond funds, over 85% went to actively managed programs**, with the balance (10%-15%) to index funds (in addition, ETFs continued to attract large flows, but mostly not from active funds – see more on page 9).

2012: By mid-February, US stock indices have erased most of the panic-driven price collapse of last summer. A slow rebound in stock fund demand is starting to show, while bond fund demand continues strong – **our industry attracted about $50 billion of bond and stock fund inflows in the first six weeks of 2012.**

- **Could the surprise in stock fund sales this year be on the up side**, despite the current malaise permeating investors' attitudes?
- Zero cash yields, risk aversion, economic uncertainty, and confidence-lowering election politics all suggest that **the insatiable search for income and safety persists in 2012. High stock dividend funds,** a theme discussed in the issue, suggests an important opportunity
- **Asset allocation solutions** continue to rise in importance.
- **Fund innovations:** a wave of new funds, away from benchmark-centric, long-biased strategies. How successfully will they meet investors' expectations?

Strategic Insight 2012: in the coming year SI will be offering a very large number of new data and research services. Among them:

- **New Simfund Data:** watch for the coming announcement of important new Simfund details regarding **granular fund data by distributor (2H 2012).** Simfund will also incorporate **new investment objectives and "flags"** to allow users to quickly conduct analysis, for example, for **"alternative" mutual funds**, as well as other evolving investment strategies. SI is also reviewing the **"distribution channel" designations in Simfund for revision**
- **Simfund Australia** is being launched
- **A new sub-advisory module** allows monitoring such opportunities across all industry's segments (all funds including VAs)
- **Pathfinder 2.0:** SI has been rolling out this service which helps financial advisers close more DC business and retain their current book

Studies and Advisory: New research services -

- **Dedicated Practice Areas:** Distribution, DC, ETFs, and fund innovations (note our recent InnovationWatch and DC Market Review). And more from FRC, now an SI subsidiary

aiCIO.com: a sister publication uniquely serving CIOs is increasingly used by mutual fund PMs and CIOs (the recent issue included an interview with Bridgewater's CEO, and discussions about low volatility, commodities, risk parity, AM scale, and much more). Check it out: http://www.ai-cio.com/

Lastly, mark your calendar: SI Fund Trends, SI's annual conference, is scheduled for June 19-20 in NYC. Speakers include key distribution execs from Merrill Lynch, Morgan Stanley Smith Barney, Ameriprise, and more. Last year this sold-out event attracted 160 investment management executives from 80 fund firms and distributors. More details coming soon, or reach out to Loren Fox, loren@sionline.com.

Strategic Insight US Fund Research Editorial Board

Avi Nachmany, avi@sionline.com, (212) 944-4451

Sonia Mata, sonia@sionline.com, (212) 217-6947 Loren Fox, lfox@sionline.com, (212) 217-6912

Dennis Bowden, dbowden@sionline.com, (212) 217-6895 Bridget Bearden, bbearden@sionline.com, (212) 217-6907

US-Based Domestic Funds: 2011 Review

Adam Feldstein
(212) 217 6935
afeldstein@sionline.com

Susan Belle
(212) 217 6948
susan@sionline.com

Fund Industry Overview
(Excludes ETFs and VA Underlying Funds)

	Net New Flows $B			
	2009	2010	2011	Q4'11
US Equity/Hybrid	-26.8	-48.9	-84.2	-52.4
Int'l Equity	41.2	72.3	34.3	-15.9
Total Equity	***14.4***	***23.4***	***-49.9***	***-68.3***
Taxable Bond	281.1	214.2	128.9	35.0
Muni Bond	69.1	10.5	-12.9	9.5
Total Bond	***350.3***	***224.8***	***116.0***	***44.5***
Total Equity & Bond	***364.7***	***248.2***	***66.1***	***-23.8***
Money Market	-505.5	-509.2	-134.6	60.6
Total Industry	***-140.9***	***-261.0***	***-68.5***	***36.8***

Source: Strategic Insight Simfund MF; Note: Flow figures exclude all funds-of-funds.

After what seemed to be a good start for domestic equity flows in 2011, renewed concerns about global economic growth in the second half of 2011 overturned investors' optimism. First-half net inflows of $22 billion to US Equity/Hybrid funds gave way to $106 billion in net outflows in the second half – resulting in net outflows of $84 billion for the year, the worst year for net outflows since 2008 (net outflows of $136 billion). Nevertheless, there were individual successes. Some 341 actively managed, open-end US equity funds each attracted over $100 million of net inflows in 2011.

Increasing European uncertainty triggered sharp NAV declines in Q3 and net redemptions for International/Global equity funds during Q4 2011, for the first time in the past 11 quarters. (For more on international funds, see page 6.)

For the full year 2011, long-term mutual funds drew $66.1 billion in total inflows (excl. ETFs), roughly one-quarter of 2010's take. While significantly slower than the pace in 2010, bond funds continued to attract strong inflows in 2011, partly in a search for yield (especially amid near-zero yields in money funds) and partly due to investors' cautious outlook. Taxable bond fund inflows dropped from $92 billion in H1 2011 to $37 billion in H2 2011 due to a slowdown in Q3 (while Q4 flows rebounded strongly). Meanwhile, muni bond funds saw net outflows for the full year, but flows went from negative in 1H to positive in 2H as worries about states' and municipalities' finances eased.

Institutional investors continued their exodus from zero-yielding money market funds in 2011, with MMF aggregate net redemptions of $135 billion in 2011. But money funds took on "safe haven" status in the fourth quarter of 2011 (following the volatile Q3), resulting in net inflows of $61 billion.

Active US equity funds' average return of -1.6% in 2011 fell shy of the S&P 500's gain of +2.1% (dragged down by the weaker performance of smaller cap funds as well as their allocations to international stocks).

Avg. Asset-Weighted Annualized Returns Pct., Active Mutual Funds

	2009	2010	2011	Q4'11
US Equity *	32.1	16.4	-1.6	10.0
Int'l Equity	38.3	13.1	-10.9	5.0
Taxable Bond	19.9	8.9	4.4	2.1
Muni Bond	17.9	2.1	9.9	1.9
Money Market	0..31	0.08	0.05	0.01

** Includes hybrid/allocation funds. Sources: Strategic Insight Simfund MF; Morningstar. Excludes ETFs and funds-of-funds.*

Although the worst of the economic crisis seems to be over, investors remain worried and sales of equity funds has been trending down in 2H. The pace of stock fund redemptions, except for a brief spike in August 2011, continued at its normalized pace of around 2%, or a bit higher, as the graph below shows.

Redemptions as a % of Assets, 11/91-11/11 Equity/Hybrid Funds (Excluding VAs and ETFs)

Source: Strategic Insight Simfund TD (ICI Trends)

Equity / Hybrid Funds: Active vs. Passive (excl. VAs & Closed-End Funds)

	Net New Flows $B		
	2009	2010	2011
Actively Managed Funds	-15.0	-17.1	-92.9
Index Funds (non-ETF)	29.0	37.1	38.2
ETF Open-End Funds	57.5	75.4	58.7
ETFs structured as UITs / Grantor Trusts / ETNs /Other	10.0	6.7	9.9

Source: Strategic Insight Simfund MF

Equity index and open-end ETFs continued to draw investors' interest. On the bond side, actively managed funds drew substantially greater net inflows.

Bond Funds: Active vs. Passive (excl. VAs & Closed-End Funds)

	Net New Flows $B		
	2009	2010	2011
Actively Managed Funds	322.3	193.5	98.8
Index Funds (non-ETF)	25.9	27.3	16.3
ETF Open-End Funds	46.2	29.6	43.9

Source: Strategic Insight Simfund MF

Growth vs. Value

For the full year 2011, core and value (including equity income) styles in open-end domestic equity funds saw net outflows. Growth eked out small net inflows; large-cap growth was the only style to realize positive flows. Naturally, **many individual higher-performing value and growth funds continued to attract significant inflows.**

Open-End Domestic Equity Fund Flows by Investment Style from 2001 through Dec 2011

Source: Strategic Insight Simfund MF; Lipper Inc. (Classifications)

Flows and returns among diversified, actively managed US equity funds are summarized in the next table.

Actively Managed Diversified U.S. Equity Flows and Performance (excl. VAs)

	Flows $B		2011
	2010	2011	Returns *
Large-Cap Growth	-13.6	1.8	-2.0%
Multi-Cap Growth	-9.3	-2.6	-1.9%
Mid-Cap Growth	-1.9	-5.9	-3.6%
Small-Cap Growth	-0.5	-0.2	-1.4%
Growth Funds	***-25.3***	***-6.9***	***-2.1%***
Large-Cap Core	-40.6	-69.4	-1.0%
Multi-Cap Core	-6.1	-5.9	-3.0%
Mid-Cap Core	2.4	-4.4	-4.9%
Small-Cap Core	-0.6	-6.9	-2.6%
Core Funds	***-44.9***	***-86.5***	***-1.8%***
Large-Cap Value	-8.7	-15.4	-1.4%
Multi-Cap Value	-1.3	-13.2	-5.2%
Mid-Cap Value	-2.4	-2.6	-2.4%
Small-Cap Value	1.9	-1.3	-4.2%
Value Funds	***-10.5***	***-32.6***	***-2.9%***

** Weighted by ending assets; Source: Strategic Insight Simfund MF; Lipper Inc. (Classifications and Returns)*

Funds with Highest Inflows: Some Risk-Return Characteristics

The decision to invest in a particular fund or with a particular fund manager is based on numerous factors, but SI has observed that **trailing three-year rankings, within the fund's investment style and on both relative-return and relative-risk dimensions, offer predictive value for flows.** Relative total returns remain the chief determinant for fund selection**.**

SI's "Bubble" charts, generated in Simfund, plot funds on a relative risk/return basis versus similarly invested peers. Funds in the top-left quadrant have superior positioning relative to peers, displaying below-average risk (defined as cumulative monthly losses over 36 monthly observations) while achieving above-average returns. And **2011** was another period for which the top-left quadrant of graphs often housed the highest-inflow funds (very recent underperformance of a few high-selling bond funds weakened their relative position in the graph by year-end).

As an illustration of cash flow results for 2011, we capture below the "trailing three-year risk-return vs. cash flow bubbles" of the industry's 40 highest cash flow funds in 2011 (trailing 3-year risk and return as of year-end measured within each fund's Lipper investment classification). Simfund subscribers can easily replicate these graphs for their peer funds (and can run such graphs within the funds' Morningstar

category as well). **Note that bubble size corresponds to 2011 net inflows.**

The funds in the charts clearly share appealing risk-return characteristics for the 36 months ending December 2011. The few outliers are funds from respected managers benefiting from a "halo" effect, hard-to-classify funds, or those reflecting strong performance in earlier periods.

Risk-Return Characteristics of Best Selling Mutual Funds in 2011

Highest Net Inflow Equity Funds in 2011 (Actively Managed, Open-End Funds) *

**2011 Flows and 3-Yr. Risk/Return Analysis within Lipper Classifications; Source: Strategic Insight Simfund MF*

Highest Net Inflow Bond Funds in 2011 (Actively Managed, Open-End Funds) *

**2011 Flows and 3 Year Risk/Return Analysis within Lipper Classifications; Source: Strategic Insight Simfund MF*

2011 Flows by Manager

The tables below present the managers making the most cash flow progress in 2011 in active, long-term funds.

All Equity and Bond Actively Managed Funds (excl. VAs and ETFs): Highest Cash Flow Managers in 2011

Manager	Flows ($B) 2010	Flows ($B) 2011	2011 Flow Rate*	12/11 Assets $B^
PIMCO	64.2	**25.3**	6%	460.4
JPMorgan Funds	20.8	**17.6**	15%	136.6
DFA	9.2	**16.5**	13%	132.1
DoubleLine Capital	4.0	**12.4**	302%	17.2
BlackRock	15.3	**10.7**	6%	173.5
MainStay Funds	2.1	**9.4**	32%	38.1
T. Rowe Price	12.4	**9.2**	4%	256.7
Franklin Templeton	20.2	**8.8**	3%	342.9
TCW / MetWest	4.3	**7.3**	28%	34.1
First Eagle	4.1	**7.0**	17%	47.5
Thornburg	9.0	**5.8**	13%	48.1
Virtus Invsmt Ptnrs	1.6	**5.6**	33%	23.0
Lord Abbett	7.7	**5.3**	8%	69.5
Pacific Heights	3.8	**5.3**	51%	15.5
Yacktman	2.9	**4.8**	89%	10.7
Prudential Financial	3.3	**4.6**	12%	40.7
MFS	5.3	**3.7**	4%	87.3
TIAA-CREF	3.2	**3.5**	15%	25.3
American Century	2.5	**3.4**	5%	78.5
Waddell & Reed	3.9	**3.2**	5%	64.2

**Flow rate = 2011 flows as a pct. of 12/10 assets; ^Active long-term assets only; Source: Strategic Insight Simfund MF*

Fastest Growing Managers: Actively Managed Long-Term Funds (excl. VAs) ^

Manager	Flows ($B) 2010	Flows ($B) 2011	2011 Flow Rate*	12/11 Assets $B**
DoubleLine Capital	3.8	10.7	**273%**	15.2
Yacktman	2.9	4.8	**89%**	10.7
Transamerica	1.6	1.4	**68%**	3.6
MainStay Funds	1.0	6.7	**55%**	18.7
Pacific Heights	3.8	5.3	**52%**	15.4
TFS Capital	0.1	0.6	**51%**	1.7
Credit Suisse	1.1	1.6	**44%**	4.7
First Pacific Advisors	1.3	3.1	**32%**	13.1
Aberdeen Asset Mgmt	1.4	2.0	**30%**	7.5
Intl Value Advisors	4.2	2.7	**30%**	11.2

*^ $1B+ in AUM at 12/10; * Flow rate = 2011 flows as % of 12/10 AUM; ** Active long-term assets; Source: Strategic Insight Simfund MF*

US-Based International Funds: 2011 Update

Adam Feldstein
(212) 217 6935
afeldstein
@sionline.com

Susan Belle
(212) 217 6948
susan
@sionline.com

US-Based International/Global Equity Mutual Funds $ Billion

Structure/Type	Assets $B 12/11	Net Flows, $B 2009	2010	2011	Q4'11
Open-end Active	1,355	33.6	56.6	13.6	-20.0
Open-end Indexed	118	9.7	19.0	17.6	3.2
ETFs*	321	53.9	49.4	23.8	5.9
Closed-End	33	0.0	0.7	1.2	0.0
VA Funds	192	7.1	7.9	4.5	3.2
Total	**2,019**	**104.3**	**133.6**	**60.7**	**-7.7**

*Source: Strategic Insight Simfund MF / VA. Data include Gold funds and ETFs; *ETFs include ETPs, UITs & open-end ETFs.*

Eurozone uncertainty and the US dollar's recovery relative to the euro helped lead to net outflows from active International/Global equity funds in the second half of the year. But ETFs and index funds helped offset those outflows, **resulting in net inflows of $60.7 billion for the full-year**.

Emerging Markets, as well as International and Global Multi-Cap programs, benefitted from inflows.

Int'l Equity , US Equity, and World Bond Funds Annual Average Total Returns (Asset-Weighted)

	2008	2009	2010	2011	Q4'11
U.S. Equity*	-37.9	31.5	16.8	-1.3	10.9
Int'l/Glbl Eqty	-41.9	40.5	13.7	-12.0	4.7
World Bond^	-1.2	15.6	9.3	0.9	1.1

*Source: Strategic Insight Simfund MF; * Exc. Balanced/Hybrid, Int'l Equity includes Gold. ^ Morningstar category.*

Although they narrowed the gap in Q4, international / global funds underperformed US equity funds in the full-year 2011 by more than 10% – a sizable margin.

The relative performance of the EAFE (vs. the S&P 500) and the recovery of inflows since 1993 are captured in the chart below:

Relative Performance of US v. Foreign Stocks, Net Flows into Int'l/Global Equity Mutual Funds

Source: Strategic Insight Simfund MF, Standard & Poor's Int'l flows include Gold funds

Again, actively managed emerging markets funds topped the list of highest-flow classifications for Q4 2011, as well as the full year. For 2011, emerging markets had more than triple the net inflows of the #2 classification, International Multi-Cap Value. Flows to international/global equity funds continue to be helped by investors' search for more global diversification.

Actively Managed Int'l/Global Equity Funds 10 Highest 2011 Net Flow Classifications

	Net Flows $B Q4'11	2011	Assets $B 12/11
Emerging Markets	1.6	15.8	165.5
Intl Large-Cap Value	1.2	0.6	35.9
Global Multi-Cap Core	0.8	1.9	9.4
Intl Multi-Cap Core	-0.2	3.7	41.3
Intl Multi-Cap Value	-0.2	4.3	34.5
Japanese	-0.0	0.2	1.6
Intl Sm/Mid-Cap Value	-0.2	0.0	9.3
Global Multi-Cap Growth	-0.3	-0.3	7.5
Intl Sm/Mid-Cap Growth	-0.4	-0.0	19.4
Global Multi-Cap Value	-0.8	0.6	21.4

Source: Strategic Insight Simfund MF; Excludes index funds and ETFs, as well as VA funds.

With the 11% underperformance of international vs. US stock funds during 2011 (the worst gap in a decade), European uncertainty, and US stocks' recent positive momentum, we anticipate the secular trend of global diversification to modestly slow down this year.

Growth Opportunities in Latin America

Daniel Enskat
+1 212 217 6859
daniel@sionline.com

Bryan Liu
+852 2251 8246
bliu@sionline.com

Latin America's mutual fund industry could reach between $2.8 and $3.6 trillion in assets by the year 2020, while its pension fund assets could approach $3 trillion — a total of more than $6 trillion, depending on the global market environment in the coming years.

With more than $1.4 trillion in local and cross-border assets currently, the size of the Latin American fund industry is comparable to that of Asia — or the US back in the 1990s. Furthermore, our data show about $850 billion in pension fund assets, with various stages of external asset management opportunities by country. We see a range of between 10% (Brazil) and 80% (Chile) of possible offshore investments. Early on, smaller markets (like Chile) looked to diversify their asset base; in contrast, large domestic markets (like Brazil) are only slowly opening up to cross-border investments (via pension funds and multimercado investments).

Latin American fund management is as concentrated as Asia-Pacific: In Latin America, Brazil and Mexico stand out as the largest domestic markets. However, Chile, Peru, and Colombia have a large proportion of UCITS pension fund assets allocated to international fund firms. In the Asia-Pacific region, Australia and Japan dominate via local structures, with Hong Kong, Singapore, and Taiwan acting as UCITS havens. Similar to Brazil, Australia has a domestic focus and protective investment environment.

Target market selection: Latin America has a number of markets that are smaller or less business-friendly that will likely only be targeted by international fund managers over time as those countries improve, and as business sustainability is ensured. For instance, a firm like Barclays UK with the acquisition of Lehman Brothers Sudamérica added Argentina teams, but has trouble finding product providers on the ground.

Roughly 90% of regional assets are in Brazil, and those assets are dominated by fixed income and multimercado (absolute return) products – due to the interest rate environment: the central bank's benchmark interest rate is still above 10%. This is in contrast to the asset class landscape seen in other markets in the region, where equities hold a larger slice.

The breakdown of the region's assets is illustrated in the following table

Latin America AUM and 5-Year CAGR by Market

In $ US Billion

	2006	2007	2008	2009	2010	5-Year CAGR	2011**
Brazil*	517	668	628	710	889	18%	**984**
Mexico	63	75	60	70	99	16%	**100**
Chile	18	24	18	34	38	22%	**34**
Colombia	n/a	7	9	13	16	n/a	**16**
Argentina	6	7	4	4	5	7%	**6**
Peru	n/a	4	2	5	6	n/a	**6**
Costa Rica	1	1	1	1	3	28%	**3**
Bolivia	n/a	n/a	1	1	1	n/a	**1**
Total*	***605***	***787***	***722***	***839***	***1,056***	***19%***	***1,150***

** Brazil figures exclude Offshore Funds and pension funds.*
*** Brazil and Chile reflect latest data available from Q2'2011; Other markets reflect data as of Q1' 2011*
Source: Strategic Insight, Investment Company Institute, FIAFIN, ANBIMA, AAFM

Memo: Cross-border funds account for an additional $200 billion in assets, pension funds across multiple markets are an additional $840 billion (that includes about $80 billion in cross-border fund vehicles) thus bringing total AUM in the region to over $2 trillion.

Over time, industry observers expect interest rates in Brazil to decline and equity investments to grow. Latin America tripled its fund assets from $500 billion to $1.4 trillion since 2005, primarily driven by Brazil/Mexico and the growth in Chile, Peru, and Colombia. However, while other markets are small in nature, they can still be an asset-gathering opportunity for international fund managers as a hub. Uruguay, for example, sits between Brazil and Argentina and is used by HNW investors as the Monaco of the region (Punta del Este is seen as the Latin American Côte d'Azur) — global financial institutions have billboards all over the country and existing global distribution relationships can be leveraged for asset-gathering purposes through international booking centers.

Latin America is not immune to the current global market volatility and economic downturn, as Brazil's

BOVESPA index dropped 18% and Mexico's IPC index declined by 4% in 2011. However, compared to markets in the US and Europe, Latin America could recover more quickly from the current crisis. Many countries in the region have stronger economic fundamentals, including low debt levels, high international reserves, and trade surpluses, as well as rich natural resources and a 600 million-strong (and relatively young) population. Indeed, Latin American countries have successfully weathered the 2008 credit crisis and have emerged stronger – the Brazilian and Mexican stock markets matched or exceeded their 2007 pre-crisis levels in 2010.

The Latin American mutual fund industry, as shown in the next chart, suffered a small setback during the 2008 crisis, but subsequently has grown rapidly to exceed $1.1 trillion in 2011 — a 55% increase compared to the previous peak in 2007. This is attributable partly to the fixed income domination in Latin American mutual funds, and local currency appreciation against the US dollar. Our research suggests that the region could see a similar decline in AUM this year, and then should continue to grow strongly and reach or exceed $3 trillion by 2020, based on a compound annual growth rate (CAGR) of about 10% for the next 10 years.

Latin American Mutual Fund AUM Projection 2005 – 2020

Source: Strategic Insight estimates

Above we show asset projections through 2020, given the current market environment: Starting with a short-lived AUM decline in 2011 similar to 2008, we see a strong foundation for growth in the region through 2020. The graph shows three possible scenarios:

- **Scenario A/Conservative Assumption** – This scenario supposes a continued economic and financial crisis in the US and Europe, and a prolonged economic slowdown worldwide. Net flows in Latin America would remain low, averaging $40 billion per year (50% below actual 2010 levels), and long-term fund returns would run at 6% per annum (including currency effects), with the industry still doubling AUM to $2.1 trillion by 2020 (a CAGR of 6%);
- **Scenario B/Average Assumption** – Governments and central banks globally would work together to contain or dampen the current crisis in a timely manner. Annual average flows in Latin America could remain at similar levels as achieved during 2010, at about $70-75 billion per year. Paired with an annual return of 7% for long-term funds, total Latin America fund assets could approach $2.8 trillion by 2020 (corresponding to a CAGR of 9%);
- **Scenario C/Optimistic Assumption** – The global economic and financial crisis would be contained quickly and markets rebound. In Latin America, long-term fund returns average 8%-9% a year, flows in 2012 and 2013 remain below 2010 levels due to continued investor uncertainty, but rise rapidly in subsequent years and average $100 billion per year for the next decade. Mutual fund assets in Latin America would more than triple and move towards $3.6 trillion by 2020, supported by continued strong economic growth and high returns in the region. This scenario shows a CAGR of 12%.

Pension fund acceleration in Latin America: In addition, pension funds in Latin America could further stimulate growth. At year-end 2010, total pension assets in the region stood at around $850 billion, or 17% of GDP ($4.97 trillion). In comparison, the pension assets-to-GDP ratio was 104% in the US, 103% in Australia, 102% in the UK, and 64% in Japan in the same year, according to Towers Watson's *2011 Global Pension Asset Study*. If the ratio in Latin America were to double and reach 33%-34% in the next decade (a moderately conservative projection), total pension assets in the region would more than triple, to reach or exceed $3 trillion by 2020 (assuming a GDP growth rate of 6-7% per annum for Latin America). Moreover, should governments continue to increase offshore investment participation, addressable pension assets could be a trillion-dollar industry for international fund managers. Clearly, a locally appropriate strategy is needed to gain market share. While there are a few very large pension funds to be targeted in a market like Chile or Peru, Brazil, with 26 states (plus one federal district) and 4,974 municipal districts, has hundreds of small local pension funds (with hundreds of millions in assets each).

More details can be found in Strategic Insight's new in-depth study, *State of the Asset Management Industry – Latin America*.

ETF Update: 2011 US ETF Flows Top $100B

Loren Fox
(212) 217-6912
lfox@sionline.com

Exchange-Traded Funds in the US drew net new flows of $40.4 billion in the fourth quarter of 2011. That raised the full-year 2011 net flows to $115 billion – marking the fifth straight year that US ETFs drew at least $100 billion in net inflows. **At the end of 2011, US ETF assets (including ETNs) totaled $1.06 billion** in 1,372 different products.

ETFs: By Investment Type

	Assets	Net Flows $B			# of
	$B 12/11	2010	2011	Q4 2011	Funds 12/11
US Equity					
Diversified	379.5	11.2	28.9	18.2	258
Sector	139.8	17.7	18.7	4.7	302
Subtotal US Equity	**519.4**	**28.9**	**47.6**	**23.0**	**560**
Int'l/Global Equity					
Diversified	69.2	5.6	13.5	1.6	73
Divrsfd Emerg Mkts	82.3	24.9	0.2	4.8	34
Regional	13.3	0.8	-2.1	0.1	27
Single Country	53.3	6.0	0.8	-3.4	96
Subtotal Int'l/ Global Equity	**218.1**	**37.3**	**12.4**	**3.0**	**230**
Total Equity	**737.5**	**66.3**	**60.0**	**26.0**	**790**
Bond					
Taxable Bond	170.2	25.0	42.7	14.3	115
Muni Bond	8.2	1.1	0.9	0.7	29
Subtotal Bond	**178.4**	**26.1**	**43.6**	**15.0**	**144**
Specialized					
Alternative Strategy	3.6	3.4	1.3	0.5	64
Commodity	104.1	12.2	-0.2	-0.1	99
Currency	6.4	-2.2	1.1	-0.1	30
Leveraged/Inverse	31.7	5.0	9.1	-0.9	245
Subtotl Specialized	**145.9**	**18.3**	**11.4**	**-0.6**	**438**
Total	**1,061.8**	**110.7**	**115.0**	**40.4**	**1,372**

Source: Strategic Insight Simfund MF

In the fourth quarter of 2011, domestic equity ETFs led the way in net inflows, in large part due to combined net flows of $8.1 billion to the SPDR S&P 500 ETF and the PowerShares QQQ. Diversified emerging markets ETFs had a strong Q4'11 ($4.8 billion in net flows), mostly due to a rebound in inflows to the iShares MSCI Emerging Market Index ETF.

Bond ETFs also turned in a strong Q4, taking in $15 billion in net inflows. Flows to intermediate-term and high-yield bond ETFs led the way, with combined net inflows of $9 billion.

US Equity ETFs did well in the full-year 2011, with net inflows of $47.6 billion. Taxable bond ETF net flows were nearly as strong, at $42.7 billion, buoyed by investors' search for yield and some investors' cautious approach to the markets. But leveraged and inverse ETFs drew a healthy $9 billion in net inflows in 2011.

One criticism of the ETF market is that it is littered with tiny ETFs. It's true that 518 (or 38%) of the 1,372 ETFs on the market at year-end 2011 held less than $20 million in assets. But 2011 saw only 18 ETFs shuttered (although that excludes 10 other ETFs whose closings were announced in December).

Only a small portion of ETF growth may be coming directly from redemptions out of mutual funds. Indeed, a **Schwab** study of ETF use from Q1 2009 through Q2 2011 found that among its retail investor clients, only 15% of net flows into ETFs came from mutual fund holdings, while 72% came from cash. In many portfolios, investors are increasingly choosing to invest new capital into ETFs rather than individual stocks and bonds. Among separate accounts, another Schwab study found that assets in all-ETF portfolios on its platform rose 30% from Dec. 2010 to Nov. 2011. **Actively managed ETF portfolios are emerging as an important source of growth.** One indication: **Morningstar** found that in the managed portfolios it tracks which are 50%+ invested in ETFs, assets increased by 43% between Sept. 2010 and Sept. 2011.

Actively Managed ETFs

Actively managed ETFs – those ETFs not aiming to exactly match an index – comprise a small segment of the ETF market. At the end of 2011, there were 42 active ETFs managing a total of $3.7 billion. That's less than ½ percent of the ETF market, and the five biggest funds held 81% of all active ETF assets.

There are six active ETFs with $100 million or more in assets. And 18 of the 42 ETFs have less than $20 million in assets. The active ETF market is waiting for new products and new entrants. We expect the first active ETFs from State Street and Legg Mason in 2012. And all eyes will be on PIMCO's announced Total Return Bond ETF, managed by Bill Gross, slated to debut March 1.

Biggest Actively Managed ETFs, Dec. 30. 2011

ETF	Assets $MM 12/30/2011
PIMCO Enhanced ShortMaturity Strategy	1,803
WisdomTree Dreyfus China Yuan ETF	449
WisdomTree Dreyfus Emerging Currency	344
WisdomTree Managed Futures Strategy	272
Active Bear ETF	154

Source: Strategic Insight Simfund MF

Non-transparent? Many traditional fund managers eyeing the active ETF market are put off by the requirement that actively managed ETFs must, like passive ETFs, disclose daily their prior-day's portfolios. They worry that such transparency carries too much risk of front-running and free-riding. Two proposed non-transparent approaches are noteworthy.

In September, **BlackRock** filed for permission to launch active ETFs which disclose their portfolios in the same manner as mutual funds rather than daily; the ETFs would effect creations and redemptions for cash via a blind trust, so the custodian would know the holdings and help generate a daily NAV, but not the Authorized Participants (the market makers who create the ETF shares that trade on exchanges). Separately, **Eaton Vance** is developing what it calls "exchange traded managed funds" which would operate like active ETFs but would disclose portfolios monthlyor quarterly, and the creation/redemption basket would differ from actual holdings. "ETMFs" would base all trades off the day's closing NAV. The SEC, already with a very full plate, is not likely to rule on these new models any time soon – but they are worth monitoring.

New ETF Launches 2011

The pace of ETF launches remained even in the fourth quarter, with **59 new ETFs in Q4** – after 59 new ETFs launched in Q3. Looking at the full year, 2011 saw a significant increase in ETF listings. In all, **308 new ETFs debuted in 2011**, drawing $10 billion in aggregate net inflows. That was an increase from 2010, when 223 new ETFs launched, drawing total net inflows of $9 billion.

The 10 most successful debuts in 2011, from eight different managers, represented a diverse set of asset classes, from US large cap to international stocks, emerging markets bonds, managed futures, and more. The **PowerShares** S&P 500 Low Volatility ETF is the most successful of a new wave of alternatively-weighted equity index ETFs. **Vanguard**'s entry is the ETF share class of its 16-year-old index fund.

Top New ETFs in 2011, By Net Flows *

ETF	Strategy	Net New Flows $MM 2011
iShares High Dividend Equity	Large Value	859
PowerShares S&P500 Low Vol	Large Value	841
Vanguard Total Intl Stk Index	Int'l Total Return	526
WisdomTree Asia Local Debt	EmrgMkts Bond	393
WisdomTree Managed Futures	Mngd Futures	299
PowerShares Senior Loan	Floating Rate	199
Schwab US REIT ETF	Real Estate	188
MAXIS Nikkei 225 Index ETF	Japan Equity	183
Active Bear ETF	Bear Market	167
SPDR S&P EmergMkts Divdnd	Emerging Mrkts	167

**Excl. HOLDR conversions; Source: Strategic Insight Simfund MF*

This Top-10 list excludes Market Vectors ETFs from **Van Eck** that debuted in December but were adoptions of HOLDRs from Merrill Lynch; HOLDRs were ETF-like vehicles with fixed baskets of stocks that Merrill discontinued in 2011. Van Eck converted the six largest HOLDRs to ETFs, taking much of their assets via exchange offers – making them "new" ETFs but not comparable to completely new ETF launches.

Biggest ETF Managers

The US ETF market is concentrated: at year-end 2011, **BlackRock, State Street and Vanguard together managed 83% of the assets.** The Top 10 ETF managers run 95% of the assets.

Top 10 ETF Managers, Dec. 30, 2011

Manager	Assets 12/30/11 $B	Market Share 12/30/11	Net Flows 2011 $B
BlackRock (iShares)	448.1	42.2%	29.4
State Street Global	257.6	24.3%	19.4
Vanguard	170.9	16.1%	32.6
InvescoPowerShares	44.7	4.2%	4.3
Van Eck	23.5	2.2%	8.0
ProFunds	23.1	2.2%	6.2
WisdomTree	12.2	1.2%	3.7
DB Commodity Svc	11.8	1.1%	0.9
Amer Stk Exchange	8.9	0.8%	-3.2
Rydex	7.7	0.7%	0.2
Top 10 Total	***1,008.4***	***95.0%***	***101.7***

Source: Strategic Insight Simfund MF

The ETF market is (very) gradually fragmenting as it grows larger and more of the assets are flowing to newer, smaller managers. For example, the top three firms' combined market share of 83% is down from 86% three years ago. There are now 47 firms operating ETFs, 23 of which manage $1 billion+ in ETF assets.

Record Flows into Income-Oriented US Stock Funds

Sonia Mata
(212) 217 6947
sonia@sionline.com

Income-focused US stock funds captured a record $30 billion in net flows in 2011, against a backdrop of continuing net redemptions in aggregate from long-only open-end US equity funds. In a low Treasury-yield, slow economic-growth, and high-volatility environment, investors have looked to dividend-focused stocks as a conservative way to participate in equities, while also earning additional income.

The current **dividend yield** of the S&P 500 Index of 2.14% is higher than what a 10 year Treasury yields now (less than 2%). The SI objective "Income & Growth" also had the highest **total return** in 2011 of all diversified US Stock fund objectives, recording +3.58% (asset-weighted average), relative to the S&P 500 Index's +2.11%. The objective had a three-year beta relative to the S&P 500 of 0.83 (average, asset-weighted).

Selected Mutual Fund Sectors and "Income & Growth"
Open-End Funds; Excludes VAs

SI Objective	12-Mth Yld %*	SEC Yield*	Total Return %* 2011	Assets $B 12/11	Net Flows $B 2011
Utilities	**2.97**	2.68	13.89	26.4	6.0
Real Estate	**2.76**	2.56	7.05	76.2	4.7
Income & Growth	**2.69**	2.64	3.49	298.9	29.6
Financial Sector	**2.07**	3.49	-18.17	18.4	-1.9
Misc. Sectors	**1.67**	0.39	1.85	28.4	1.4
Natural Resources†	**1.63**	1.45	-8.28	71.5	2.3
Gold†	**1.47**	4.31	-20.08	38.5	1.6
Health	**1.45**	1.41	10.19	44.5	1.6
Technology	**1.09**	0.86	-4.22	36.9	0.3

** Asset-weighted average. †Only stock funds; excludes commodities funds. Source: Strategic Insight Simfund MF*

Flows into the "Income & Growth" objective showed an uptrend starting in October 2010 as risk appetites began to recover and some investors used these types of funds to dip their toes back into equity waters. Momentum didn't slow even after last summer's volatility. The record volume in 2011 came despite ongoing uncertainty as to whether the special 15% tax rate on dividends instituted as part of the Bush era tax cuts in 2003 would continue beyond 2012.

Income & Growth Funds*: Annual Flows, $Billion

** Open-end funds and ETFs, excluding VAs. Source: SI Simfund MF*

Notably, more than half of last year's $30 billion net flow total into the "Income & Growth" area came within conventional (non-ETF) funds, which, save for three offerings (two from Vanguard, and one new one from Guggenheim), are all actively managed. This was a turnaround from the experience in each of the prior three years, when "Income & Growth" conventional funds were in net redemptions, and it was income-focused stock index *ETFs* that were attracting growing flows.

Income & Growth Funds
Open-End Funds and ETF; Excludes VAs

	Assets $B	Net Flows $B		
	12/11	2009	2010	2011
Conventional Funds	264	-8.6	-2.7	**15.7**
ETFs	35	1.6	8.0	**13.8**
Total above	***299***	***-6.9***	***5.3***	***29.5***

Source: Strategic Insight Simfund MF

In terms of sector allocations, the average "Income & Growth" fund had the most assigned to Industrials (14.5%), Consumer Defensive (14.4%), Energy (12.3%), Healthcare (12%), and Financial Services (10.9%), on an asset-weighted basis.

Income & Growth Funds*: Sector Allocations†

** Open-end funds and ETFs, excluding VAs. †Asset weighted average of latest available sector allocation data from Morningstar.*
Source: Strategic Insight Simfund MF

Top Selling Conventional "Income & Growth" Funds in 2011

The ten conventional (non-ETF) open-end funds that led the "Income & Growth" space in terms of net flows in 2011 were all actively managed funds.

Highest Flow "Income & Growth" Funds in 2011
Open-End Funds; Excludes ETFs and VAs

Portfolio Name	Assets $B 12/11	Net Flows $B 2010	Net Flows $B 2011	Total Rtrn % 2011	12mth Yld %
BlackRock Equity Dividend	17.5	3.2	**5.5**	5.60	1.87
Federated Strtgc Value Dividend	5.5	1.1	**2.8**	14.48	3.60
Vanguard Dividend Growth	7.7	1.5	**2.5**	9.43	2.03
Columbia Dividend Income	4.8	0.7	**1.6**	6.96	2.43
American Century Equity Income	9.4	0.9	**1.4**	3.57	2.66
Prudential Jennison Eqty Inc	2.2	0.7	**1.3**	-0.40	3.49
Neuberger Berman Equity Inc	2.0	0.5	**1.3**	4.85	2.78
T. Rowe Price Equity Income	21.5	0.6	**1.2**	-0.72	1.95
Vanguard Equity Income	6.6	0.2	**1.2**	10.60	2.78
JPMorgan Equity Income	1.3	0.0	**1.0**	7.59	2.02

Source: Strategic Insight Simfund MF

BlackRock's $17.5 billion **Equity Dividend** fund maintained the flow leadership position it has held among "Income & Growth" funds in each year since 2008, with a largest-ever annual net intake of $5.5 billion in 2011. This large-cap oriented fund aims to pick stocks that it believes will both increase in value over the long term and provide current income, instead of giving preference to current income over capital appreciation. The fund returned 5.6% in 2011 and had a 12-month yield of 1.87% as of December-end. It has one of the lowest turnover ratios (5% over the latest fiscal period) in the "Income & Growth" space. The fund has been positioned in recent years to seek indirect gains from the growth of the middle-class in emerging markets through allocations to the equity income stocks of US firms exposed to EM countries. This theme was reflected at the end of 4Q'11 in an overweight to the materials, industrials and consumer staples sectors relative to the fund's benchmark, the Russell 1000 Value Index. Conversely, its PMs' beliefs as to the challenges confronting US consumer spending resulted in an underweighting of the consumer discretionary, financials and healthcare sectors as of December-end.

Federated's $5.5 billion **Strategic Value Dividend** more than doubled its flows last year relative to 2010, and jumped a spot in the flow rankings, assuming second position with net flows of $2.8 billion. The fund invests chiefly in high dividend-yielding, undervalued stocks with dividend growth potential. Its 14.5% total return in 2011 was the second-highest of all open-end "Income & Growth" conventional funds; its 3.6% 12-month yield as of December-end was the sixth-highest in the segment; and its three-year beta versus the S&P 500 Index came in at 0.68—the eighth-lowest in the area. The fund screens and ranks stocks based on quantitative statistics, and uses mainly bottom-up fundamental research to assess the subset of highly ranked companies for including in the portfolio. Macro trends that can affect sector/industry outlook are also taken into account. At the end of December, this large-cap oriented fund's sector allocations were led by Consumer Staples (28% of the fund's assets), Healthcare (21%), and Telecom (20%), and its holdings numbered 42.

Vanguard's Dividend Growth fund took in a net $2.5 billion last year, putting it in third position among all "Income & Growth" conventional open-end funds in terms of net flows. Sub-advised by **Wellington**, the fund seeks large-cap, high-quality companies that are attractively priced and have the potential for growing dividends over the long-term rather than those with a long dividend-paying past record. In addition, it looks for capital appreciation potential and current income. The fund generally invests in a concentrated portfolio of about 50 dividend-paying stocks. At the end of 2011, it had the most exposure to the health care (16%), consumer staples (15.1%), industrials (14.5%), and information technology (14.5%) sectors. Another large-cap, dividend-focused fund from Vanguard that features in the top-10 sellers list, the **Vanguard Equity Income**, seeks stocks with above-average *current* income and reasonable long-term capital appreciation potential; co-managed by Wellington and Vanguard, this fund typically holds about 160 stocks.

New Fund Launches: Big Debuts in 2011

Tony DiSanzo
(212) 217 6951
adisanzo@sionline.com

New funds face a unique challenge in drawing investor capital. Recently launched mutual funds cannot highlight a fund's performance history or its ratings, so managers must take a different tack. A review of the most successful (by net inflows) funds launched in 2011 shows that many of them rode ongoing currents in product innovation and demand to attract inflows.

The highest-flow new fund in 2011 was American Funds's Global Balanced fund (benefitting from pent-up demand among the firm's clients; we estimate that among all of the manager's funds, gross sales exceeded $100 billion in 2011, but redemptions were greater). Morningstar classifies it as World Allocation, a category which includes many of the newly incepted global tactical asset allocation (GTAA) funds. SI tracks new fund registrations through its SimfundFiling.com tool, and GTAA was a popular theme throughout 2011, due to demand for global exposure and more tactical (and perhaps more nimble) approaches to investing. As the table below shows, the World Allocation category saw the most fund launches last year and the second-highest volume of net new flows.

Mutual Funds: 10 Highest Net-Inflow Categories, 2011

Morningstar Category	2011 Net New Flows $B	New Funds in 2011
Intermediate-Term Bond	33.6	9
World Allocation	25.4	44
World Bond	22.6	7
Diversified Emerging Mkts	18.6	31
High Yield Bond	14.1	10
Bank Loan	13.7	11
Conservative Allocation	11.9	5
Emerging Markets Bond	11.7	19
Short-Term Bond	10.3	5
Nontraditional Bond	9.4	12

Data excludes ETFs and VA funds
Source: Strategic Insight Simfund MF

With investors in search of higher yield (or any yield at all), four the 10 biggest fund launches of 2011 (by net inflows) were fixed income funds – as the table below shows. Bank loan funds were a popular strategy; 11 of these portfolios were introduced last year, and the Goldman Sachs High Yield Floating Rate Fund, launched in March, saw inflows of $578M through December. In the same vein, the High Yield Bond category saw 10 new fund launches last year.

Highest Net-Inflow Mutual Funds Launched in 2011

Fund	2011 Net Inflows $B	Launch Month	Category
American Glbl Balanced	2.92	Feb	World Allocation
JHF II Cap Apprectn Val	1.03	Jan	Mod Allocation
Fidelity Conserv Inc Bond	0.69	Mar	Ultrashort Bond
PIMCO Total Return IV	0.67	May	IntermTerm Bond
PIMCO EqS Emerg Mkts	0.60	Mar	Divsfd Emerg Mkts
GS Hi Yield Floating Rate	0.58	Mar	Bank Loan
MassMutual RetireSMART Moderate Fund	0.54	Jun	Mod Allocation
JPM Floating Rate Inco	0.47	Jun	Bank Loan
MassMutual RetireSMART Moderate Growth Fund	0.41	Jun	Aggr Allocation
ING International Core	0.40	Feb	Foreign Lg Blend

Data excludes ETFs, closed-end funds, and VA funds.
Source: Strategic Insight Simfund MF

The GMO Emerging Markets Opportunity Fund, launched in April, just missed the top 10 with $398M in net inflows in 2011.

This list includes some of the biggest asset managers, so distribution networks and strong brands surely played a part in the funds' success. PIMCO, for example, had net inflows of $23B in 2011 spread across many funds. But it is clear that the highest flow new funds also tended to be in the most popular categories. Moreover, in most cases no single fund dominated the inflows for these categories, so the success was widely shared. Funds launched into these categories were able to take advantage of prevailing investor sentiment and grab some of the inflows.

Seen broadly, the fund launches in 2011 also show that the secular shift towards global and emerging markets products has continued. Two of the three Morningstar categories which saw the most mutual fund launches last year were World Stock and Diversified Emerging Markets, each with 31 new funds. And the Emerging Markets Bond category was tied for sixth with 19 new funds.

Closed-End Funds: The Market Evolves

Loren Fox
(212) 217-6912
lfox@sionline.com

The US closed-end funds market took advantage of some significant tailwinds in 2011. The industry-wide demand for income-oriented products provided a good context for closed-end funds, which are used mainly for income, and investors' increasing acceptance of non-traditional asset classes was reflected in closed-end fund IPOs. **Last year, 17 closed-end funds came to market, raising $5.6 billion in aggregate.** It was a decline from the $7.4 billion raised in 17 IPOs in 2010, but up from the depths of 2008-09, when a combined $2.7 billion was raised in 16 IPOs.

Median Closed-End Fund Discounts to NAV, June 2008 – December 2011

Source: Lipper Inc.

Sentiment toward closed-end funds has improved since 2009, spurring contractions in market-price discounts to NAV, but stock and bond CEF discounts took a divergent path in 2011. As the graph above shows, discounts for equity CEFs worsened while discounts for fixed income CEFs improved last year, as volatility and economic angst returned in 2011. Performance was also a factor – muni CEFs, which make up 34% of closed-end fund assets, gained an asset-weighted average 17% in 2011 vs. just 4% for US equity CEFs.

But the closed-end fund market has changed. Crisis-fueled consolidation among the large investment banks/brokerages has meant fewer (and pickier) underwriters for closed-end fund IPOs. Last year, the average closed-end fund IPOs raised $332 million, down from $434 million in 2010 and from $689 million in 2007. It may be that the market can no longer support the 40 to 50 closed-end fund IPOs per year that were routine in 2003-07.

The good news is that there are still opportunities for distinctive closed-end funds – so long as they also offer an attractive yield. **Since the end of 2008, 12 new closed-end fund managers have entered the market.**

Closed-End Fund IPOs, 2011

Fund	IPO Net Proceeds $MM
BlackRock Resources & Commodities	834
Duff & Phelps Global Utility Income	701
ClearBridge Energy MLP Opportunity	522
Nuveen Energy MLP Total Return	422
ING Emerging Markets Hi Dividend Equity	367
Gabelli Natural Resources, Gold & Income	355
First Trust Energy Infrastructure	329
BlackRock Utility and Infrastructure	296
Apollo Senior Floating Rate	286
John Hancock Hedged Equity & Income	267
Tortoise Pipeline & Energy	239
Blackstone/GSO Long/Short Credit	238
Nuveen Short Duration Credit Opportunity	191
Guggenheim Equal Weight Enhnc Eqty Inco	167
Salient MLP & Energy Infrastructure	151
Brookfield Global Listed Infrastructure	150
Avenue Income Credit Strategies	129
Total: 17 IPOs	**5,644**

Source: Strategic Insight Simfund MF

As the table makes clear, the closed-end funds that came to market in 2011 tended towards less-traditional asset classes. Natural resources (especially MLPs), infrastructure and senior loans were popular. **BlackRock Resources & Commodities Strategy Trust**, 2011's biggest IPO, combines natural resources equities with covered call writing. Other notable debuts include the **Guggenheim Equal Weight Enhanced Equity Income Fund,** the first non-market cap-weighted equity CEF; and an equity CEF from John Hancock that hedges its positions by writing calls on its equities and buying puts on the S&P 500.

A rising number of innovative closed-end funds are also in the pipeline, including a fund investing in trade finance-related securities, a fund investing tactically in ETFs and other CEFs, and a fund using a liquidity algorithm. We expect to see more innovation in this space in 2012 and beyond.

QDIA Opportunities

Bridget Bearden
(212) 217-6907
bbearden@sionline.com

The DC channel offers opportunities for both investment-only asset managers as well as those with a proprietary recordkeeping business. A recordkeeping product does not, however, guarantee sales into proprietary investment options. ERISA requires plans to offer "a broad range of investment alternatives," which most plan sponsors associate with open-architecture. While asset manager/recordkeepers may have proprietary fund requirements, the plan sponsor's perception of potential fiduciary liability will continue to necessitate a minimum level of open architecture.

In aggregate (including proprietary and investment-only), 2011 DC net flows are scheduled to ring in lower than both 2009 and 2010. According to the ICI, Equity DC funds saw net outflows for the first three quarters of 2011, and Bond fund inflows were at their lowest levels post-crisis.

However, Hybrid funds (as defined by mixed equity/bond funds) have captured the lion's share of total DC net flows since 2007, and remain relatively insulated from uncertain economic conditions. Most target date and target risk funds, two types of QDIAs, reside in the ICI's 'Hybrid' classification.

DC Mutual Fund Flows ($B)

	2008	2009	2010	YTD-Q3'2011
Equity	-60	(0)	-11	-36
Hybrid	32	33	34	26
Bond	17	37	27	9
Money market	42	-28	-26	8
Total	**31**	**42**	**24**	**7**

Source: ICI

This sort of stability in net inflows – in part ensured by auto-enrollment and participant inertia – makes the QDIA an attractive objective for asset managers. While proprietary target-dates do dominate across the DC market in aggregate, there are pockets of investment-only opportunity in the QDIA space.

According to the PLANSPONSOR 2011 DC Survey, over half (54%) of plan sponsors reported that a target date fund (either active, index or custom) was the QDIA for auto-enrollment in 2011. Another 21% of plan sponsors reported using a risk-based lifestyle fund or a balanced fund as the QDIA.

Even though plan sponsors commonly use target-dates and balanced funds as QDIAs, they do not report 100% confidence in the appropriateness of particular products. This uncertainty creates an opening for asset managers to introduce their own QDIA philosophy.

In the most recent PLANSPONSOR DC survey, plan sponsors were asked which product they felt was the "Best QDIA for Employee Population: Balanced Funds, Managed Accounts, Target Dates, Not Sure, or Other." Micro and small plans were most likely to say that they were not sure which QDIA option was best for their employee population. In fact, 40% of micro plans (<100 participants) said they weren't sure. This large percentage highlights the need for education among micro and small plans, as well as an opportunity for asset managers to market new QDIA options.

DC Plan Market, Segmented by Participant Count

	<500	500-4,999	≥5,000
% of DC Assets	35%	24%	41%
% of DC Plans	97%	2%	0.5%

Source: PLANSPONSOR Recordkeeper Survey 2011

As the smaller plan markets represent an opportunity for introducing new QDIAs, the larger ends of the markets demonstrate a clear choice of QDIA winner. The level of confidence in the best QDIA grows moving up market in terms of plan size, and towards a preference for target-date. Three-quarters of large and mega plan sponsors perceive target-dates as the best QDIA for their employee population.

In 2011, just under 3% of plan sponsors indicated that they would change their QDIA by year-end. Another 8% of plan sponsors said that they weren't sure whether they would change their QDIA. As highlighted in the "Best QDIA for Employee Population" question previously, smaller plan segments exhibit the most uncertainty about the future of their QDIA. The lower end of the market is more likely to not only change the QDIA, but also to be unsure about the course of action with respect to the default.

While QDIA opportunities exist in the smaller, advisor-sold plans, the potential to capture non-QDIA assets in these segments should not be overlooked. The survey found that smaller plan sponsors, in general, were most likely to add an investment option in 2011.

PLANSPONSOR is a sister company of Strategic Insight.

Alternative Fund Demand among Discretionary FAs

Dennis Bowden
(212) 217-6895
dbowden@sionline.com

The rapidly increasing influence of discretionary account management by financial advisors within many broker-dealers, as well as via the RIA channel, has been one of the most important trends affecting the intermediary-sold marketplace over the past several years. This growth carries many important strategic implications for fund firms, from both sales and product perspectives. Among the many differentiating characteristics of discretionary advisors, one of the most notable is their greater acceptance of non-traditional strategies.

This article summarizes some of the important findings around Discretionary Rep-as-PM demand trends from the Q3'2011 version of our joint research series with Coates Analytics – *National Broker Dealer Product Strategy & Distribution Trends*. [For more information on subscription options, contact Dan Weinerman – dweinerman@sionline.com; 212-217-6897.]

As seen in the chart below, Discretionary Rep-as-PM platform structures have grown steadily since Q1'2008 within the Coates Analytics-tracked universe of National BDs – rising to 16% of total mutual fund wrap platform assets at the end of Q3'11.

Source: Coates Analytics Distribution Management System / SI Analysis

Amid the sustained volatility and high overall financial uncertainty that persists in the post-crisis period, a growing number of FAs continue to show a greater desire to manage their clients' portfolios in a more direct and tactical nature – increasingly via discretionary account structures. As fund demand among investors and FAs continues to evolve with regard to the composition of the "core" portfolio, the sales trends of these discretionary advisors show that many are approaching tactical management with a unique perspective.

Rethinking Traditional Portfolio Construction

The growing interest in "non-traditional", or alternative, investment strategies within the mutual fund structure has been one of the key trends shaping the overall fund industry. While such interest has come from several avenues, sales trends demonstrate that Discretionary Rep-as-PM advisors are at the forefront of implementing (as opposed to merely exploring) such alternative strategies within their clients' asset allocation portfolios.

The graph below charts Alternative Equity sales (encompassing market neutral, long-short, commodities, natural resources and bear market strategies) as a proportion of total equity fund sales within each of three platforms: Non-Discretionary Rep-as-Advisor, Discretionary Rep-as-PM and Home Office Model Portfolio-Based wrap programs (all data within the Coates-tracked universe of NBDs.

Source: Coates Analytics Distribution Management System / SI Analysis

In aggregate, Rep-as-PM advisors have consistently allocated the largest proportion of new equity fund sales to Alternative Equity funds since Q1'2008. As these discretionary platforms have grown in size, the more esoteric demand trends of such advisors have become a more significant part of overall intermediary

fund demand, as well as a more important focus for many fund firms.

While these aggregate figures are clearly telling, because of the varying guidelines for classification of "alternative" funds they may even understate the growing importance of such strategies among Rep-as-PM advisors. A more granular analysis of top-selling individual funds gives a clearer and more detailed picture of Rep-as-PM demand characteristics. The table below charts the top-10 selling US Equity funds during the first nine months of 2011 within Coates-tracked Discretionary Rep-as-PM wrap platforms.

Discretionary Rep-as-PM Platforms: Top-Selling US Equity Funds, YTD-Sept. 2011

Fund Name	Lipper Classification	% of 2011 Total Program US Equity Sales
PIMCO All Asset All Authority	Flex Portfolio	4.0%
Permanent Portfolio	Flex Portfolio	4.0%
Virtus Premium AlphaSector	Lg Cap Core	2.8%
Federated Prudent Bear	Spec Dvsfd Eq	2.4%
Wells Fgo Avtg Growth	LgCap Growth	1.6%
Rydex SGI Mgd Futures Str	Absol Return	1.5%
Yacktman Focused Fund	Lg Cap Value	1.2%
JPM Hibrdg DynComm Strtgy	Commodity	1.2%
PIMCO StksPLUS+ TR Short	Short Bias	1.1%
PIMCO CommdtyRlRtrn Strgy	Commodity	1.1%

Source: Coates Analytics Distribution Management System / SI Analysis

Eight of the top-10 selling funds (highlighted) in the table above offer some type of non-traditional investment strategy. Notably, these funds cover a wide range of non-traditional strategies – including alternative asset class exposure (such as commodities or managed futures), inverse equity exposure, as well as more flexible and tactically managed portfolios offering diversification across asset classes.

Even within the traditional US Large Cap Equity categories, Virtus Premium Alpha Sector has garnered rapid sales growth among Rep-as-PM advisors since its launch in July 2010. The fund, which is subadvised by F-Squared Investments and utilizes a tactical ETF sector-rotation strategy, fits within a broader theme of increased demand for strategies which strive to offer investors and FAs lower-volatility exposure to various segments of the market.

Increased interest in non-traditional mutual fund strategies has clearly not been limited to discretionary advisors. However, sales trends within other advisor segments have shown that such interest has not yet translated to the proportional level of actual sales as within Rep-as-PM programs. The following table charts the top-10 selling US Equity funds during the first nine months of 2011 within Coates-tracked Non-Discretionary Rep-as-Advisor wrap platforms.

Non-Discretionary Rep-as-Advisor Platforms: Top-Selling US Equity Funds, YTD-Sept. 2011

Fund Name	Lipper Classification	% of 2011 Total Program US Equity Sales
Permanent Portfolio	Flex Portfolio	2.7%
PIMCO All Asset All Authority	Flex Portfolio	2.6%
Franklin Income Series	Mix Tgt All Mod	2.2%
Wells Fargo Advtg Growth	Lg Cap Growth	2.1%
MainStay Large Cap Growth	Lg Cap Growth	2.1%
BlackRock Equity Dividend	Equity Income	1.9%
Virtus Premium AlphaSector	Lg Cap Core	1.9%
PIMCO CommdtyRealRtrn	Commodity	1.3%
Yacktman Fund	Lg Cap Value	1.3%
EatonVance Large Cap Val	Lg Cap Value	1.3%

Source: Coates Analytics Distribution Management System / SI Analysis

While non-traditional strategies did make up four of the top-10 selling US Equity funds within Rep-as-Advisor programs during the first nine months of 2011, this total accounted for only one-half as many top-sellers as within Rep-as-PM programs.

And the concentration of total US Equity sales among these top-sellers was also significantly higher within Rep-as-PM programs. The eight alternative funds highlighted in the Rep-as-PM table accounted for 18.7% of total platform US Equity sales through Q3'11. That compares to just 8.7% for the four highlighted funds in the Rep-as-Advisor table above.

Looking Ahead

As many FAs have moved toward business models which allow them greater direct control over their clients' portfolios, they have also begun to rethink these portfolios' composition. Clearly, discretionary advisors have been among the early movers to deploy non-traditional mutual fund strategies as more substantial portions of their clients' overall portfolios.

The rise in discretionary advisors, and in discretionary assets as a portion of many fund firms' ongoing businesses (and the corresponding rise in asset velocity), should continue to influence the increasing interest in non-traditional strategies across wider subsections of fund managers and the overall fund industry. Over time, the greater availability and presence of such alternative strategies within the intermediary-sold marketplace should also contribute to greater interest among advisors and investors.

529 College Savings: Retooling the Advisor Channel in 2011

Paul Curley, CFA
FRC
(617) 399-5621
paul.curley@frcnet.com

Despite the growth in assets under management for the 529 college savings industry to $135 billion at the end of the third quarter, as shown in the first graph below, the breakdown of assets under management by distribution channel has been shifting towards the direct-sold channel, as noted in the second graph to the right. To help rebuild and retool the momentum for the advisor-sold channel, it was notable that this channel saw two new market entrants in 2011. JPMorgan was able to reenter the industry as the primary distributor of New York's 529 College Savings Program (advisor-sold), while DWS made its initial introduction as primary distributor of the MOST–Missouri's 529 Advisor Plan.

529 College Savings Plan Assets, 2006-Q3'11

Source: Financial Research Corp., a division of Strategic Insight

Despite the projected trend of market participant consolidation based on economies of scale and continued fee pressure, the number appears to be rising in the advisor channel with the entrance of DWS in Q2'11 and reemergence of JPMorgan in Q3'11. Together, the two firms represent the expansion of primary distributors from 38 to 40 in the 529 industry. Their entrance is significant, as most RFPs give preference to firms with current experience with the marketplace. These tendencies also vary on a state-by-state basis, however, underscoring the fact that the 529 industry is a collection of state agencies and not one national market.

529 Savings Plan Asset Breakdown by Distribution Method, 2006-Q3'11

Source: Financial Research Corp., a division of Strategic Insight

JPMorgan was able to reenter the industry as the primary distributor of New York's 529 College Savings Program (advisor-sold). Once the transition is completed, the entrance of JPMorgan will impact the landscape of the industry based on the size of its industry assets. As the New York advisor-sold plan oversaw $1.9 billion in assets under management as of Q2'11, JPMorgan is projected to rank as the 20th-largest 529 plan distributor as of the end of the third quarter. Additionally, JPMorgan's entrance will particularly develop the bank distribution channel. JPMorgan told FRC that it believes its banking center footprint and extensive third-party intermediary network in New York State will provide residents with greater access to the 529 Plan. Indeed, FRC believes that selectively developing new 529 distribution channels such as the bank channel will help expand overall product usage into new target markets.

In addition to JPMorgan, DWS transitioned into the primary distributor role of the MOST–Missouri's 529 Advisor Plan in June 2011. DWS sought to enter the 529 industry to build up its US distribution, to be a part of the growing 529 industry, and to help advisors' planning processes by including 529 plans in DWS's current line-up of mutual funds, retirement plans and other products. Additionally, it provided the firm with a platform for its investment products. For example, the plan now carries five DWS funds with A and C share classes, such as DWS Dreman Small Cap Value. As the assets continue to grow throughout the 529 industry and as firms continue to seek new distribution channels for their products, FRC projects that additional firms will become increasingly interested in participating in its growth.

FRC is a division of Strategic Insight.

Innovation, Refocus On 2012 VA Agenda

Kevin Ng
(212) 217 6922
kng
@sionline.com

Tamiko Toland
(212) 217 6949
tamiko
@sionline.com

Jeffrey Hutton
(212) 217 6954
jeff
@sionline.com

It doesn't take a degree in finance to know that 2011 was a challenging year, with uncertainty in global markets affecting both bonds and equities. For VAs, the stresses reached a new pitch when the Fed announced it would leave interest rates at historic lows and, to add insult to injury, embarked on "Operation Twist." With VA guarantees heavily dependent on long-term fixed interest rates, the collapse of yields across the yield curve was unwelcome news. Plus, continued equity volatility means it isn't exactly easy to back VA guarantees.

The fundamental conundrum for annuity manufacturers is that the unfavorable environment for the instruments that support guarantees (fixed and variable alike) also increases the demand for these products. These conflicting realities will continue in 2012.

Elsewhere, industry evolution is bringing a whole new set of strategies aimed at RIAs and non-VA sellers.

2011: The Year That Was

In the face of continued economic challenges, several insurers backed away from VA manufacturing. Genworth, at the beginning of the year, announced a shut-down of all variable products.

More recently, two companies added their names to the list: Manulife and Sun Life, both leading Canadian players. Although these decisions are similar on their face, Sun Life has taken more austere measures in completely ending all sales of VAs and life insurance in the U.S., while Manulife continues to maintain a limited presence.

Even many companies that didn't elect to ramp down sales have taken a more cautious approach to VAs, designing products to their own risk-management comfort rather than entering the competitive melee. As a result, we see continued concentration in the marketplace among three players: Jackson National, MetLife, and Prudential.

Yet initiatives to expand the reach of VAs are far from over, and we have seen new RIA-geared products trickling onto the market.

Perhaps more interestingly, standalone living benefits (SALBs) are starting to make a comeback. First, it was in the form of an in-plan product from Great-West, originally launched in 2010. The company registered a retail version during 2011. More recently, Aria Retirement Solutions, in partnership with Transamerica, is targeting advisors with an open - architecture SALB.

2012: More Innovation

The coming year is going to bring with it another wave of innovation; call it post-crisis 2.0. If the immediate response to the crisis was panic, soon followed by experimental first steps, now is the time when the rubber meets the road.

Insurers may have hoped that the economy would rebound by now, with volatility normalizing and interest rates starting to climb. However, with more of the same on the horizon, it's clear that annuity manufacturers must have a sustainable strategy for this type of environment, not simply limp through until the sun breaks through the clouds.

Despite the increased popularity of immediate annuities, these products alone are clearly not the answer. Low interest rates (and, therefore, returns) have turned a lot of consumers off from these products, leaving them with few appetizing options.

Jackson National ended 2011 with two filings that possibly herald the tidings of the New Year. The SEC approved a new VA that offers no guarantees whatsoever. In addition, it registered a novel living benefit that features a non-life guarantee.

The importance of the non-life component cannot be understated, as it is the longevity insurance component of GLWBs that is the source of so much risk management angst. Does this mean that Jackson National has had a change of heart regarding GLWBs? With its flagship VAs on the market, no. However, diversification helps reach new customers and helps the actuaries/balance sheet. We expect more new ideas keeping – and bringing – insurers in the game.

Strategic Insight

Learn how over 250 investment managers and related companies benefit from their Strategic Insight Partnerships

Global Research

Global service used by over 70 of the world's largest asset managers

US Registered Mutual Funds

Fund research suite used by managers of 90% of the US fund industry's total assets

Variable Annuities/VA Funds

VA research suite used by a great majority of industry participants

Database and Web-Based Services

Simfund GL
Global Database

- Track over 30,000 funds in Europe/Offshore and 20,000 funds in Asia and Australia
- Provide a global perspective on fund flows and trends
- Cover more than 20 key markets throughout the world
- Monthly Flows, Assets, Performance, Ratings, Fees

Asia FlowWatch

Monthly: Highest Selling Funds, Newest Funds, Innovations, Investment Demand by Country and Across Region

Simfund MF
Mutual Fund Database

- Used by managers overseeing 85% of industry assets
- Training on demand
- Sub-advisory mapping
- Fee benchmarking
- Monthly cash flows and assets
- Lipper, Morningstar, SI: One Platform

SimfundFiling.com

- SEC: Daily Fund Changes
- New Fund Registrations
- New Prospectus Data Profile
- Customizable email alert
- Instantly connect between Simfund and each fund's SEC Filings
- Weekly and monthly synopsis

Data Feeds

Compliance Assistance

Private Label Simfund

Simfund VA
Variable Annuity Database

- Monthly assets and net flows
- Comprehensive sub-advisory data and analytics
- Performance and risk data
- Fee benchmarking

AnnuityInsight.com
Daily and Weekly Synopses of VA innovations

- Daily tracking VA filings with the SEC
- Weekly write-ups of industry trends
- Essential for contract design

Research and Consulting Services

StrategicInsightGlobal.com
For Investment Companies Worldwide

- Monthly flow data on fastest growing funds in Asia and Europe
- Research and consulting on more than 20 countries
- In-depth analysis of Industry Developments
- Opportunities for Marketing and Distribution
- Product Development Ideas and Benchmarking

SIonline.com

- Online Library of On-Going Reports
- Past studies since 1994 archived
- Trends, Product, Distribution, Fees

Fee and Expense Consulting

- Interpreting the Data
- Analytical Integrity
- Hard to Find Historical Data
- Integration with SEC Edgar

Consulting

Industry Trends, Strategy, Marketing and Distribution, On-line Industry Briefings

On Demand Research

Responsive Solutions for your information needs

Board of Director Services

- Prism Review: 15(c) Analytics (Advisory Contract Renewal)
- On Demand Reports

Variable Annuity Consulting

- Library of VA research reports
- On-site industry trend presentations
- Contract feature trends
- Best practice analytics on targeting sub-advisory opportunities

To learn more, visit www.SIonline.com, www.StrategicInsightGlobal.com, www.SimfundFiling.com, www.AnnuityInsight.com

For additional information, contact Rita Leytush, [212 944 4466, rita@sionline.com]