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POOR PERFORMANCE OF MUTUAL FUNDS IN SPAIN 1991-2007

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Abstract

During the past 10 to 16 years, the average return on mutual funds in Spain was lower than the average return on government bonds at any term. During the past 10 years, the average return on the funds was lower than inflation. In spite of these results, on December 31, 2007, 8,264,240 investors held 238.7 billion Euros in the 2,907 existing mutual funds. During 2007, the number of shareholders descended by 555,569 and the value of their assets dropped by 6.1%.

Only 30 of the 935 mutual funds with 10-year history outperformed the benchmark, and only two of them outperformed the overall index of the Madrid Stock Exchange (ITBM).

If the return of every mutual fund in the past 16 years had not been the one obtained but instead the benchmark of its category, the appreciation of the funds over 1992-2007 would have been €180 billion, instead of the €80 billion they achieved. The total of fees and other expenses for the period ascended to €34 billion.

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POOR PERFORMANCE OF MUTUAL FUNDS IN SPAIN 1991-2007

We analyze the return on Spanish mutual funds over the 1991-2007 period.

Table 1 shows the main characteristics of mutual funds in Spain. As of December 31 2007, 8,264,240 investors held €228,299 million in the 2,907 existing mutual funds. During 2007, the number of shareholders descended by 555,569 and the value of their assets dropped by 6.1%.

What is surprising is the large number of existing funds and their spread.

Table 1

Main Characteristics of Spanish Mutual Funds, 1991-2007

	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Value of assets (€ billion)	**23.2**	**37.8**	**61.6**	**67.6**	**73.3**	**112**	**162**	**204**	**206**	**183**	**180**	**171**	**198**	**220**	**246**	**254**	**239**
Number of funds	374	480	579	663	752	959	1.458	1.867	2.154	2.426	2.540	2.487	2.623	2.654	2.616	2.779	2.907
Shareholders (millions)	1.15	1.68	2.55	2.79	2.94	4.29	6.24	7.98	8.01	7.66	7.45	7.13	7.63	8.04	8.56	8.82	8.26
Holdings/fund (€ millions)	62	79	106	102	97	117	111	109	95	76	71	69	75	83	94	92	82
Holdings/holder (€ thousands)	20	23	24	24	25	26	26	26	26	24	24	24	26	27	29	29	29

In **Table 2**, we compare the average return on mutual funds in Spain during the past 3, 5, 10 and 16 years (4.03%; 3.81%; 2.22%; 4.54%) with inflation, stock market investment and Spanish government bonds. It is surprising that, over the past 10 years, mutual funds did not achieve sufficient results to cover the loss of value due to inflation. In fact, average return on the funds over the last 10 and 16 years was below that of state bonds at any term.

Note: The authors are thankful for the observations made on previous editions of this paper by Manuel Andrade, León Bartolomé, Juan Palacios and Ignacio Pedrosa.

Table 2

Comparison of Return on Spanish Mutual Funds and Other Magnitudes

	Annual average return of the period ending in December of 2007			
	3 Years	**5 Years**	**10 Years**	**16 Years**
Mutual funds (*source: INVERCO*)	**4.03%**	**3.81%**	**2.22%**	**4.54%**
Inflation	3.2%	3.2%	3.0%	3.4%
Investment in Spanish gov. bonds:				
1 day	2.9%	2.6%	**3.2%**	**5.5%**
1 year	2.7%	2.7%	**3.4%**	**5.8%**
3 years	2.4%	3.0%	**4.3%**	**7.4%**
10 years	2.1%	4.3%	**5.8%**	**9.5%**
Investment in Spanish stock market::				
ITBM	24.5%	25.9%	13.7%	16.4%
IBEX 35 (with dividends)	22.5%	24.1%	10.4%	15.1%
IBEX 35 equally weighted*	22.2%	25.7%	13.1%	16.4%
Top 30 DIV weighted*	27.0%	26.3%	20.5%	22.6%
Top 20 Book/P weighted*	40.9%	36.5%	30.6%	30.8%

Only four of the 935 funds with at least 10 years of history provided a higher return than 12%: Bestinver stock market (18.9%), Bestinfon (17.2%), Bestinver Mixed (13.4%) and Bestinver international (12.05%). Significantly, all four of them belong to the same fund manager. twenty-six funds (seven of them guaranteed) with a 10-year history provided a negative return! The value of their assets was €803 million in December 2007.

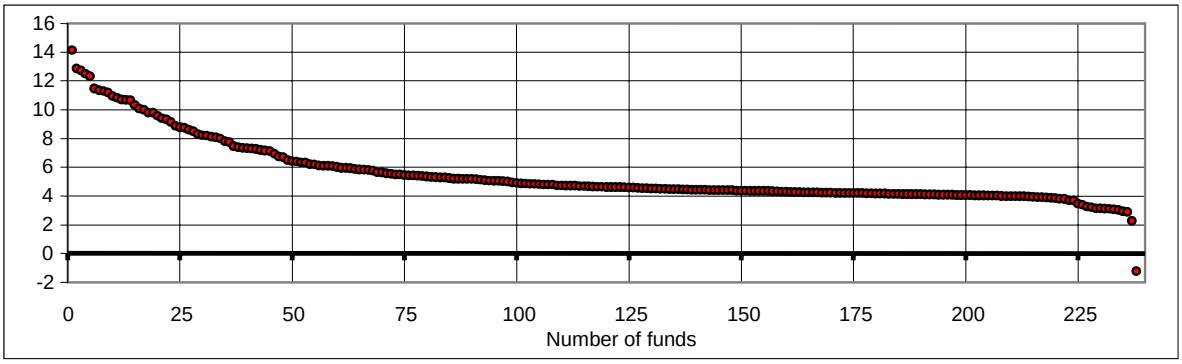
Only five of the 238 funds with a 16-year history provided a higher return than 12%: Fonbilbao shares (14.13%), Citifondo R.V. (12.86%), MS stock market (12.73%), EDM-investment (12.49%) and Metavalor (12.31%).

Figure 1 shows the return on the 238 funds with a 16-year history, from the highest (14.13%) to the lowest (-1.23%). This chart allows us to make some observations:

- 166 of the 238 funds had a lower return than 1-day Spanish government bonds.
- 201 of the 238 funds had a lower return than 3-year Spanish government bonds.
- 218 of the 238 funds had a lower return than 10-year Spanish government bonds.
- All the 238 funds had a lower return than the IBEX35 or the overall index of the Madrid Stock Exchange.

Figure 1

Return on the 238 Mutual Funds with a 16-year History

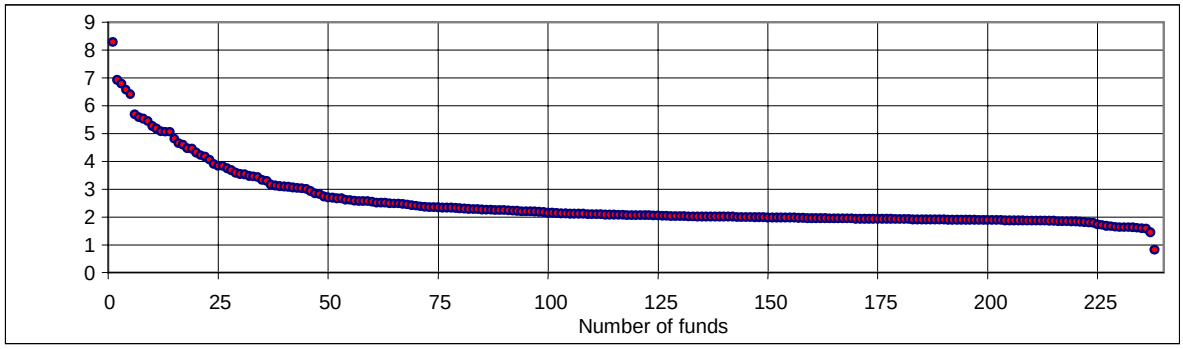


Source: Inverco

The information provided in **Figure 2** is similar to the one in Figure 1 but it is expressed in Euros: it shows how much 1 Euro invested in December 1991 in each of the funds was worth by December 2007. 1 Euro became €8.29 in the case of the most profitable fund and €0.82 in the least profitable.

Figure 2

Return in Euros on the 238 Mutual Funds with a 16-year History



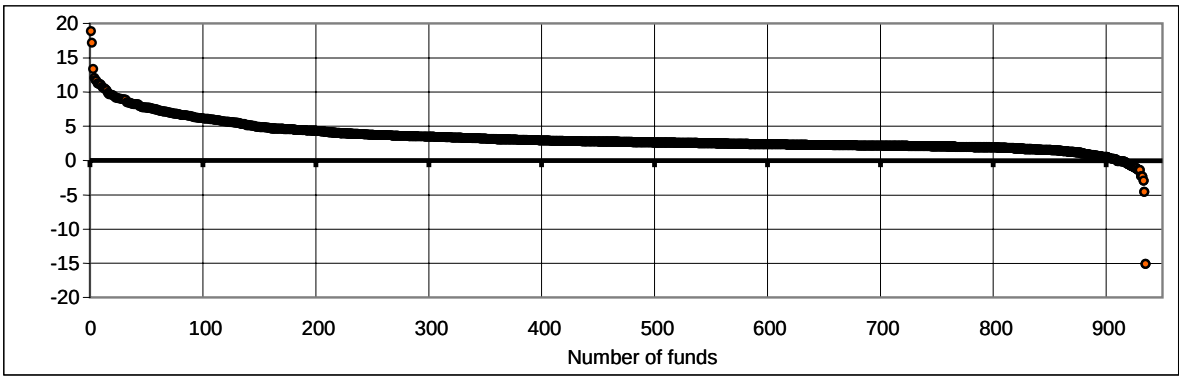
Source: Inverco

Figure 3 shows the return on the 935 funds with a 10-year history, from the highest (18.9%) to the lowest (-15.1%). This chart allows us to make some observations:

- 557 of the 935 funds had a lower return than inflation.
- 593 of the 935 funds had a lower return than 1-day Spanish government bonds.
- 736 of the 935 funds had a lower return than 3-year Spanish government bonds.
- 820 of the 935 funds had a lower return than 10-year Spanish government bonds.
- Only two of the 935 funds had a higher return than the overall index of the Madrid Stock Exchange.

Figure 3

Return on the 935 Mutual Funds with a 10-year History

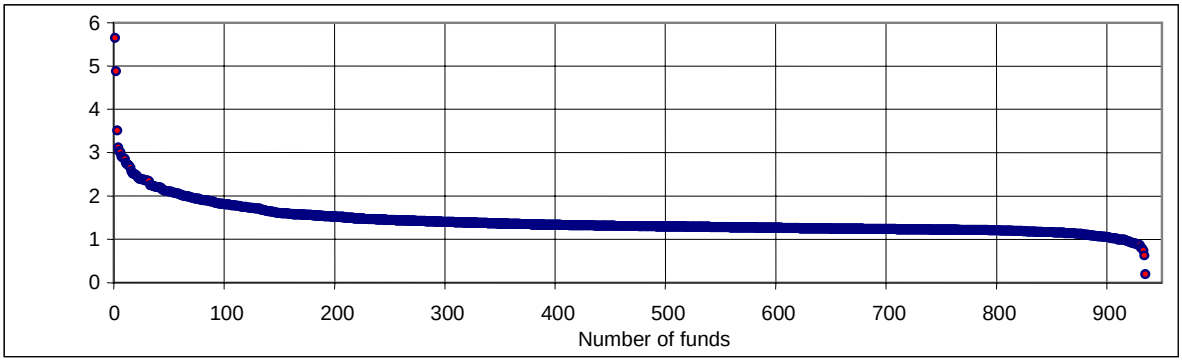


Source: Inverco.

The information provided in **Figure 4** is similar to the one in Figure 3 but it is expressed in Euros: it shows how much 1 Euro invested in December 1997 in each of the 935 funds was worth by December 2007. One Euro became €5.95 in the case of the most profitable fund and €0.19 in the least profitable.

Figure 4

Return in Euros on the 935 Mutual Funds with a 10-year History



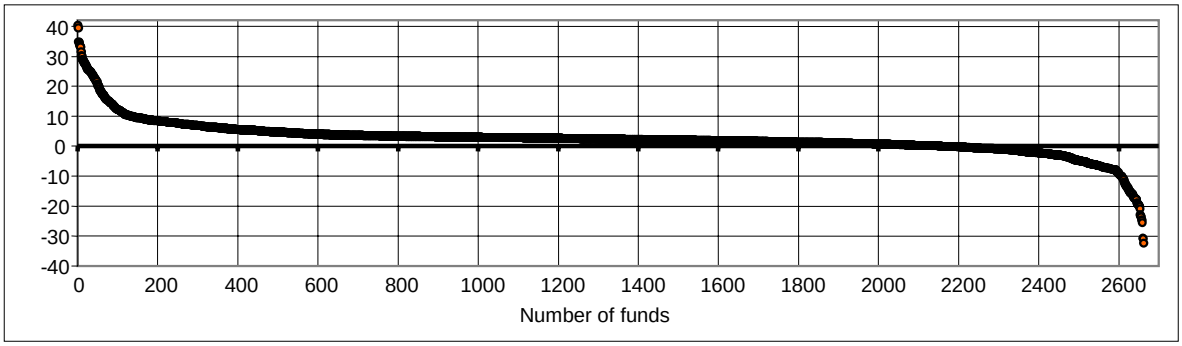
Source: Inverco

Figure 5 shows the return on the 2,663 funds that existed during 2007, from the highest (40.3%) to the lowest (-32.4%). This chart allows us to make the following observations:

- 2,105 of the 2,663 funds had a lower return than inflation.
- 519 of the funds had a negative return. 57 of them were guaranteed; 47 were international, fixed-income; 17 were long-term, fixed-income; 7 were mixed, fixed-income; and 34 were mixed equity.

Figure 5

Return on the 2663 Mutual Funds with 1 - year (2007) History



Source: Inverco

Return Analysis on Each Category of Funds

In this paper, mutual funds are grouped according to categories established by INVERCO (see **Appendix 1**). The return on the funds in each category is compared with a benchmark mentioned in Appendix 1. For example, the return on the funds falling into "National Equity Mutual Funds" category is compared to the return on the overall index of the Madrid Stock Exchange. Also, "Short-term, fixed-income" funds are up against the return of 1-day Repos.

Tables 3 and 4 sum-up this comparison. For example, the holdings of the funds belonging to the "National Equity Mutual Funds" category increased from €123 million at the end of 1991, to €7,825 million at the end of 2007. The weighted return of these funds during the last three years (2005, 2006, and 2007) was 19.5%, and during the last 16 years (from December 1991 until December 2007) was 11.5%. The annual average return of ITBM during the three years was 24.5% (5% more than the average of the funds), and during the last 10 years it amounted to 13.7% (5.6 more than the average of the funds).

According to **Table 4**, from the 122 National Equity Mutual Funds that existed at the end of 2007, only 16 were created more than 16 years ago, 61 of them had 10 years of history, 90 had five years and 104 had three years. None of the 16 funds with a minimum of 16 years of history had a higher return than the benchmark. None of the 61 funds with a minimum of 10 years of history had a higher return than the benchmark. Only two of the 99 National equity mutual funds with a minimum of five years of history had a higher return than the benchmark.[1]

[1] A paper analyzing the return on Spanish equity mutual funds can be downloaded from: http://ssrn.com/abstract=985120

Table 3

Historical Return on Mutual Funds to Shareholders and Difference with the Benchmark

		Holding billions of €		Historical return to shareholders (%) until 2007				Return differential (%) Historical - Benchmark			
		1991	2007	3 Years	5 Years	10 Years	16 Years	3 Years	5 Years	10 Years	16 Years
Fixed Income	**Short-term**	15.53	92.3	2.15	2.0	2.43	4.40	-0.7	-0.6	-0.8	-1.1
	Long-term	4.85	6.4	1.2	1.8	2.63	4.78	-1.1	-1.8	-2.4	-3.7
	Mixed	1.30	8.3	4.0	4.2	2.73	5.17	**-4.0**	**-5.1**	**-4.9**	**-5.7**
Equity	**Mixed**	0.42	6.3	9.2	9.2	3.77	6.54	**-8.8**	**-10.1**	**-7.8**	**-7.9**
	National	0.12	7.8	19.5	21.2	8.11	11.49	**-5.0**	**-4.7**	**-5.6**	**-4.9**
Internat.	**Fixed income**	0.26	0.9	0.5	1.0	2.22	4.84	-2.7	2.4	-1.2	-3.5
	F. income Mixed	0.47	4.7	3.0	2.7	2.25	4.60	-2.8	0.2	-2.8	**-5.1**
	Equity Mixed	0.05	2.7	5.8	5.8	1.79	5.56	**-4.6**	-3.3	**-4.8**	**-5.7**
	Variable Euro	0.10	7.7	13.8	13.2	4.25	8.84	**-9.1**	**-10.5**	**-8.5**	**-7.3**
	Variable Europe	0.01	5.7	12.6	11.8	3.40	7.21	-1.2	-1.2	-2.5	**-5.5**
	Variable USA	0.01	0.8	4.3	4.2	0.47		-1.1	-1.0	-2.2	
	Variable Japan	0.00	0.4	3.1	5.4			**-6.6**	**-5.1**		
	Variable Emerging	0.01	2.1	32.0	28.1	9.02	9.40	0.7	0.0	-1.9	-3.7
	Variable Rest	0.01	4.5	9.4	8.6	0.24	4.85	**-7.6**	**-7.7**	**-7.8**	**-7.5**
	Global	0.09	27.7	3.7	3.6	1.88	5.07	**-13.3**	**-12.7**	**-6.2**	**-7.3**
Guaranteed	**Fixed income**		18.1	1.8	2.1	2.93		-0.7	-0.8	-1.0	
	Equity		42.2	3.6	3.6	3.93		**-5.1**	**-5.6**	-2.1	
	TOTAL of FUNDS	**23.2**	**238.7**	**4.03**	**3.81**	**2.22**	**4.54**	**-3.2**	**-2.7**	**-2.2**	**-2.2**

Weighted return (IRR) of all mutual funds from the year indicated until 2007

1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
3.5%	3.5%	3.4%	3.1%	3.1%	2.9%	2.6%	2.3%	1.8%	***1.4%***	2.0%	2.6%	3.8%	3.8%	**4.0%**	3.7%	2.4%

Table 4

Number of Funds for each Period and Number of Funds with a Higher Return than the Benchmark

		Number Funds Dec. 2007	Number of funds for the period until 2007				Number of funds with historical return higher than the			
			3 Years	5 Years	10 Years	16 Years	3 Years	5 Years	10 Years	16 Years
Fixed Income	**Short-term**	386	330	280	216	87	2	7	2	1
	Long-term	144	128	115	90	32	11	7	**0**	**0**
	Mixed	136	129	121	80	28	6	2	**0**	**0**
Equity	**Mixed**	144	138	127	87	28	**0**	**0**	1	**0**
	National	122	104	90	61	16	1	2	**0**	**0**
Internat.	**Fixed income**	65	51	44	24	8	2	30	2	**0**
	F. income Mixed	76	65	55	16	6	7	40	**0**	**0**
	Equity Mixed	79	70	68	24	6	4	6	**0**	**0**
	Variable Euro	119	99	88	33	7	**0**	2	2	**0**
	Variable Europe	71	54	47	14	2	16	17	2	**0**
	Variable USA	43	38	32	5		5	10	2	
	Variable Japan	25	20	19			2	3		
	Variable Emerging	59	40	36	10	2	14	14	1	**0**
	Variable Rest	159	137	128	24	2	9	7	1	**0**
	Globals	423	246	169	75	14	7	5	2	**0**
Guaranteed	**Fixed income**	262	145	100	65		9	6	5	
	Equity	594	386	289	111		32	9	10	
	TOTAL of FUNDS	**2,907**	**2,180**	**1,808**	**935**	**238**	**127**	**167**	**30**	**1**

Table 5 reflects the volatility of the returns on funds falling into each category. For example, if we analyze the return on the 104 National Equity Mutual Funds with a 3-year existence, the fund with the highest average return reached 28.2% while the fund with the lowest average return reached only 7.5%. The standard deviation of the 104 average returns[2] was 3.1%. The benchmark (the return of ITBM) reached a 24.5%.

Figure 6 is a graphic representation of this dispersion and shows the maximum, minimum and average (weighted) returns on each category.

The dispersion of the returns on each category is dependent on the investment decisions of the fund managers, on fees and expenses, and on the investment philosophy of the fund. The latter refers to the fact that some categories include very different funds. For instance, the category "International, Variable Emerging" includes funds with such different names as "Bric, New Challenges," "Eastern Europe," "China," "Ibero America" and "Asia." The category "International, Equity Europe" includes funds such as small & mid caps, active market, dividend, telecommunications, UK, Switzerland, real estate, quantitative, profit, solidarity dividend, euroindex, special situations and research.

Table 5

Average Return on Mutual Funds over the past Years

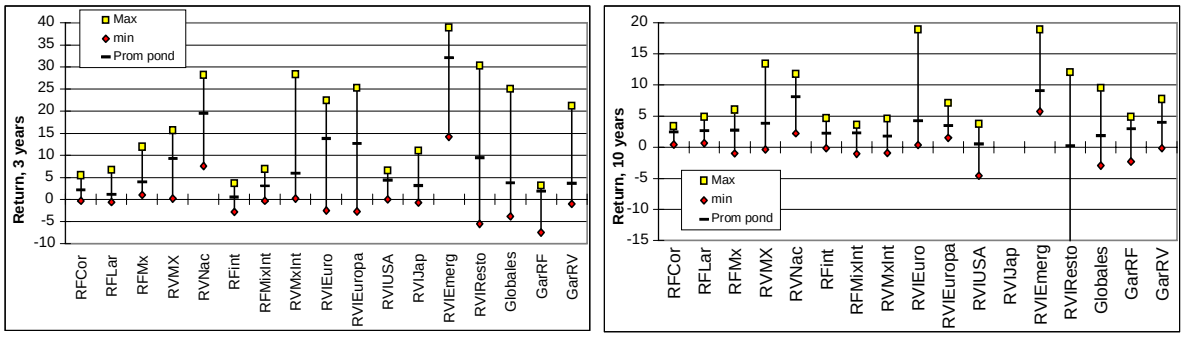
The table shows, for each category, the maximum and minimum returns, the standard deviations (σ) of the returns and the benchmark

		3 years				5 years				10 years				16 years			
		MAX	**min**	**σ**	benc	**MAX**	**min**	**σ**	benc	**MAX**	**min**	**σ**	benc	**MAX**	**min**	**σ**	benc
Fixed Income	Short-term	5.43	-0.32	0.5	2.89	3.2	-1.6	0.5	2.6	3.4	0.4	0.4	3.2	5.8	3.1	0.4	5.5
	Long-term	6.63	-0.62	0.8	2.24	8.6	0.4	1.1	3.7	4.8	0.6	0.7	5.1	6.4	3.9	0.6	8.5
	Mixed	11.96	1.06	1.7	7.95	13.2	1.0	1.7	9.3	6.0	-1.0	1.1	7.6	7.3	3.7	0.8	10.8
Equity	Mixed	15.64	0.25	3.1	17.97	17.8	0.5	3.3	19.3	13.4	-0.4	2.3	11.6	11.2	2.9	2.1	14.4
	National	28.20	7.53	3.1	24.50	26.3	8.9	3.0	25.9	11.7	2.2	1.9	13.7	**14.1**	7.8	1.9	16.4
Internat.	Fixed income	3.62	-2.85	1.4	3.19	6.8	**-6.2**	3.5	-1.3	4.7	-0.1	1.3	3.5	5.3	3.1	0.9	8.4
	F. income Mixed	6.88	-0.34	1.6	5.84	7.7	0.5	1.5	2.5	3.5	-1.1	1.2	5.0	6.2	2.3	1.5	9.7
	Equity Mixed	28.33	0.21	4.5	10.42	27.5	0.8	4.4	9.1	4.6	-0.9	1.6	6.6	8.0	3.1	1.6	11.2
	Variable Euro	22.47	-2.51	3.6	22.88	26.9	0.5	4.2	23.8	**18.9**	0.3	4.3	12.8	10.0	2.9	2.6	16.2
	Variable Europe	25.25	-2.76	4.2	13.82	27.8	6.1	4.6	13.0	7.1	1.5	1.8	5.9	11.4	9.4	1.4	12.7
	Variable USA	6.56	0.02	1.7	5.35	14.0	-0.3	3.7	5.2	3.7	-4.6	3.7	2.7				
	Variable Japan	11.03	-0.72	3.2	9.72	15.1	1.9	3.9	10.5								
	Variable Emerging	**38.86**	14.1	**5.4**	31.30	**35.4**	8.8	5.9	28.0	11.7	5.7	2.0	11.0	11.3	10.	0.4	13.1
	Variable Rest	30.26	-5.51	5.5	16.98	26.8	-2.8	4.9	16.3	12.1	-	4.6	8.0	7.3	3.9	2.4	12.4
	Globals	25.08	-3.81	4.9	16.98	23.3	-1.9	4.8	16.3	9.5	-2.9	2.2	8.0	10.3	**-1.2**	2.7	12.4
Guaranteed	Fixed income	3.1	**-7.51**	1.0	2.55	3.5	***-3.5***	0.8	2.8	4.9	***-2.3***	0.9	3.9				
	Equity	21.25	-0.99	3.1	8.75	20.8	***-0.3***	2.5	9.2	7.7	***-0.1***	1.4	6.0				
	TOTAL of FUNDS	**38.86**	**-7.51**		7.7	**35.4**	**-6.2**		7.1	**18.9**	-		5.2	**14.1**	**-1.2**		7.5

[2] The standard deviation of the average returns measures the dispersions of the resulted returns. If all the funds in a category had the same return, the standard deviation would be zero. The higher the standard deviation, the higher the dispersion of the returns. It can be observed that the categories with higher dispersion (volatility) were "Variable, Emerging"; "Variable, Rest"; "Variable, Euro," "Variable, Europe." The categories with the least dispersion (volatility) were "Short Term, Fixed Income" and "Long Term, Fixed Income."

Figure 6

Mutual Funds Return in the past 3 and 10 Years



Average return, 3 years **Average return, 10 years**

The Impact of the Return Differential from the Benchmark in the Capitalization and Appreciation of Mutual Funds

If the return to shareholders of mutual funds had been similar to the benchmark, what would the value of their holdings be? This is the question we now address.

The first two columns in **Table 6** reflect the equity of the funds in 1991 and 2007. The increase in the value of the total equity of the funds is due to the appreciation of the funds and to contributions (net investment) by investors over the years. Column 3 shows Net Investment (IN NET) of the shareholders,[3] and Column 4 the appreciation of the funds between 1992 and 2007 (AP hist). It is obvious that:

P2007 = P1991 + IN NET + AP hist.

Column 5 reflects how much the funds would have had appreciated if their return had been the benchmark instead of the given return. Column 6 shows what the total equity of the funds would have been in 2007 if the appreciation was the one in Column 5, instead of the historical appreciation (Column 4) and if the Net Inversion of the shareholders had equaled the historical value (Column 3). Column 7 is the difference between Columns 4 and 5 (AP hist. – AP bench), and Column 8 is the percentage Column 7 represents in Column 4.

[3] The table contains aggregated data obtained after calculations with annual data. We can use data published by Inverco in order to obtain the average return on each type of fund every year (Rt). Also, Inverso releases the value of the funds' holdings every year (Pt). Therefore, we can calculate the Net Investment of the shareholders using the following equation: IN NETt = Pt – Pt-1(1+Rt). Net Investment is the difference between the contributions and withdrawals of the investors, assuming they were all realized on the last day of the year. Appendix 3 shows how to calculate Net Investment each year.

Table 6

Value of Asset Holdings and Appreciation if the Return had been Equal to the benchmark, 1991-2006

Value of holdings 2007 = Value of holdings 1991 + Net Investment 1992-07 + Appreciation. P2007 = P1991 +IN NET + AP

(data in million €)		Value of holdings (millon €)		History of the Period 1992-2007		If return = benchmark		Difference: history vs. benchmark: AP hist – AP bench	
		P2007	P1991	IN NET	AP hist	AP bench	P 2007 bench	millon €	%
		[1]	[2]	[3]	[4]	[5]	[6]	[7] = [4] -[5]	[8] =[7]/[4]
Fixed Income	Short-term	92.254	15.529	41.635	35.089	49.071	106.236	-13.982	-40%
	Long-term	6.390	4.853	-7.817	9.353	21.826	18.863	-12.473	-133%
	Mixed	8.284	1.296	2.977	4.012	12.508	16.780	-8.496	-212%
Equity	Mixed	6.349	422	2.496	3.431	17.085	20.003	-13.654	-398%
	National	7.825	123	396	7.306	15.371	15.891	-8.066	-110%
Internat.	Fixed income	903	256	-145	792	1.677	1.789	-886	-112%
	F. income Mixed	4.733	470	2.662	1.600	6.364	9.497	-4.764	-298%
	Equity Mixed	2.708	53	2.375	280	2.555	4.983	-2.275	-813%
	Variable Euro	7.717	102	5.994	1.621	9.646	15.742	-8.025	-495%
	Variable Europe	5.703	14	4.588	1.101	1.989	6.591	-888	-81%
	Variable USA	805	5	1.151	-352	-171	986	-181	51%
	Variable Japan	443	1	1.086	-645	-540	547	-104	16%
	Variable Emerging	2.111	7	1.139	966	1.142	2.287	-176	-18%
	Variable Rest	4.462	11	7.344	-2.893	3.306	10.661	-6.199	214%
	Globals	27.707	90	25.219	2.397	11.226	36.536	-8.828	-368%
Guaranteed	Fixed income	18.110	0	13.028	5.082	6.620	19.648	-1.538	-30%
	Equity	42.192	0	31.151	11.040	20.353	51.504	-9.312	-84%
	TOTAL of FUNDS	238.699	23.234	**135.282**	80.184	180.027	338.542	-99.843	-125%

The total equity of the funds went from 23.234 billion Euros in 1991 to 238.699 billion Euros in 2007. The reasons for the increase are the contributions by investors totaling 135.282 billion Euros, and the appreciation (yield) of the funds during 1992-2007 (€80.184 billion). If the return on the funds had been equal to the benchmark for each category, the appreciation of the funds during 1992-2007 would have been €180.027 billion; that is, €100 billion more than the actual gains registered (125% more than the appreciation of the funds). Consequently, we can conclude that, from the €180.027 billion mutual funds that could have appreciated following the benchmarks we employed, the shareholders only got €80.184 billion. Using the poor historical information offered by CNMV on fees charged by mutual funds, we can calculate the total of fees and charges (explicit commissions) in 1992-2006 at €34 billion. The other €66 billion (100-34) is due to hidden commissions and investment decisions.

The difference of €92.392 billion has to do with hidden and explicit commissions[4] and with erroneous investment decisions.

Table 7 is identical to Table 6 but it focuses on the last 5 years. The yield of the funds on par with the benchmark would have brought 83.693 billion Euros during the period 2002-2007, that is, an improvement of €41.617 billion over the €42.076 billion obtained. This €41.617 billion represents 99% more than the funds actually obtained. Using the poor historical

[4] Explicit commissions are defined as those that the shareholders pay and that appear on the fund's contract as costs related to management, deposit, subscription and refund. Hidden commissions are those paid by the shareholders, which are derived from sales commissions arising when a manager sells securities and buys others. It is not possible to quantify the value of the latter because the great majority of funds do not release them.

information offered by CNMV on fees charged by mutual funds,[5] we can calculate the total of fees and charges (explicit commissions) in 2002-2007 at €13.385 billion. The remaining €28.232 billion (41.617 – 13.385) is due to hidden commissions and investment decisions.

Table 7

Period 2003–2007

(data in million €)		Value of Holdings (million €)		History of the Period 2003-2007		If return = benchmark		Difference: history vs. benchmark: AP hist – AP bench	
		P2007	P2002	IN NET	AP hist	AP bench	P 2007 bench	million €	%
		[1]	[2]	[3]	[4]	[5]	[6]	[7] = [4] -[5]	[8] =[7]/[4]
Fixed Income	Short-term	92.254	80.329	3.451	8.474	12.353	96.133	-3.879	-46%
	Long-term	6.390	10.503	-5.003	889	1.545	7.046	-656	-74%
	Mixed	8.284	6.396	388	1.499	3.359	10.143	-1.859	-124%
Equity	Mixed	6.349	6.878	-3.617	3.088	7.991	11.252	-4.903	-159%
	National	7.825	3.962	-3.817	7.679	10.224	10.370	-2.545	-33%
Internat.	Fixed Income	903	1.544	-742	101	64	866	37	37%
	F. income Mixed	4.733	7.532	-3.444	645	322	4.409	324	50%
	Equity Mixed	2.708	2.410	-575	873	1.409	3.243	-536	-61%
	Variable Euro	7.717	3.230	1.792	2.695	6.007	11.029	-3.312	-123%
	Variable Europe	5.703	2.261	1.393	2.049	2.339	5.992	-290	-14%
	Variable USA	805	691	-63	177	216	844	-39	-22%
	Variable Japan	443	380	36	27	49	465	-22	-80%
	Variable Emerging	2.111	252	800	1.059	1.032	2.085	26	3%
	Variable Rest	4.462	3.903	-1.262	1.820	3.858	6.500	-2.038	-112%
	Globals	27.707	2.409	22.736	2.562	11.873	37.019	-9.312	-364%
Guaranteed	Fixed Income	18.110	15.107	1.460	1.542	2.002	18.569	-459	-30%
	Equity	42.192	23.012	12.288	6.892	19.050	54.349	-12.158	-176%
	TOTAL of FUNDS	238.699	170.801	25.822	42.076	83.693	280.316	-41.617	-99%

Explicit Commissions of Mutual Funds

Table 8 provides all the information the authors were able to obtain after consulting CNMV and INVERCO. It might be interesting to complete Table 8, but, unfortunately, we were not able to. The English TER (Total Expense Ratio) is used more and more to refer to explicit commissions and to all the charges a shareholder has to assume.

Explicit commissions are defined as those commissions that shareholders pay and that appear on the fund's contract as costs related to management, deposit, subscription and refund. Despite their names, an important part of these commissions goes to marketing and distribution expenses. A surprising fact is that in the case of many mutual funds, the sales rep's salary is higher than the manager's.

[5] Table 1.7 of the IIC statistics available on the web page of CNMV offers data on the total of charges shareholders pay (management commissions, deposit commissions and operating expenses) for all the funds and starting in 2002. According to this table, the total charges that shareholders had to pay (as a percentage of average holdings of the funds) was 1.33% in 2002; 1.21% in 2003 and 2004; 1.2% in 2005 and 1.17% in 2006.

Table 8

Explicit Commissions as a % of the Average Value of Holdings (TER) of the Mutual Funds

		1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006*	2007
Fixed Income	Short-term															0.74%	0.52%
	Long-term															1.20%	0.86%
	Mixed															1.39%	1.08%
Equity	Mixed															1.91%	1.36%
	National															1.96%	1.40%
Internat.	Fixed Income															1.28%	0.76%
	F. Income Mixed															1.42%	1.00%
	Equity Mixed															1.65%	1.21%
	Variable Euro															2.00%	1.45%
	Variable Europe															2.20%	1.55%
	Variable USA															1.75%	1.16%
	Variable Japan															1.98%	1.51%
	Variable Emerging															2.31%	1.92%
	Variable Rest															2.07%	1.50%
	Globals															1.37%	1.00%
Guaranteed.	Fixed Income															0.79%	0.55%
	Equity															1.46%	1.11%
	TOTAL of FUNDS															1.21%	0.85%

table 1.7 **	TOTAL of FUNDS					1.55%	1.56%					1.33%	1.21%	1.21%	1.20%	1.17%	
table 2.6**	TOTAL FIM		1.80%	1.84%	1.79%	1.75%	1.66%	1.60%	1.68%	1.62%	1.54%	1.42%	1.31%	1.29%	1.27%	1.31%	
table 3.6**	TOTAL FIAMM		1.39%	1.39%	1.27%	1.36%	1.34%	1.24%	1.31%	1.17%	1.06%	1.04%	1.02%	0.99%	0.96%	0.45%	
table 5.7**	TOTAL guaranteed											1.31%	1.33%	1.43%	1.39%	1.34%	

Source: CNMV

* According to Appendix A2.2 of the December 31, 2006 CNMV (and suppressing some of the errors it contained).

** According to IIC Statistics of CNMV corresponding to several years. 1993, 1994 y 1995: Management and deposit commissions according to Tables 6.3 and 6.9 of the annual report. 2000: total operative expenses according to Cambón (2007).

Previous Studies on the Return of Mutual Funds

The most complete study is the one realized by Palacios and Alvarez (2003) who studied the return on Spanish equity mutual funds for two periods: 21 funds from 1992 until 2001, and 55 funds from 1997 until 2001. During the 1992-2001 period, while the annual average returns of ITBM and IBEX 35 were, respectively, 16.3% and 15.1%, the average return on the 21 funds was of 10.7%, and the funds with the highest return (BSN Banif ACC. Españolas and Citifondo RV) had average returns of 14.8% and 14.6%. During the 1997-2001 period, while the annual average returns of ITBM and IBEX 35 were, respectively, 15.9% and 12.4%, the average return on the 55 funds was of 8.3%, and the funds with the highest return (Chase Bolsa Plus and Bolsacaser) had average returns of 14.2% and, respectively, 13.7%. According to Palacios and Alvarez (2003), the average of the annual average management and deposit commissions over 1997-2001 was of 2.41%.

De Lucas (1998) compared the return on 36 equity mutual funds between 1992 and 1996 to the return on IBEX 35 (without considering dividends). The comparison is incorrect as he did not include the dividends in the index, but De Lucas (1998) concluded that 11 funds had a higher return than the index. During 1992-96, when the monthly average returns on ITBM and IBEX 35 were 1.42% and 1.39% respectively, the fund with the highest return (Fonventure) obtained an average monthly return of 1.80%. Besides, four other mutual funds had a higher return than the ITBM.

Ferruz, Marco, Sarto and Vicente (2004) compared the return on 40 stock or mixed mutual funds with the return on the overall Index of the Madrid Stock Exchange (without dividends) during the 1995-2000 period. They reached the conclusion that 16 of them had a higher return than the ITBM. However, all the 40 funds had a lower return than ITBM or Ibex 35 adjusted for dividends: during 1995-2000, while the 3-month average returns of ITBM and Ibex 35 were 6.9% and 6.5% respectively, the fund with the highest return (Citifondo RV) had a 3-month average return of 6.0%.

Regarding the return on mutual funds in the United States or United Kingdom, we recommend the article by Nitzsche, Cuthbertson and O'Sullivan (2006), which is a wonderful compilation of the articles published on the subject. Some of the conclusions are:

1. Less than 5% of stock mutual funds have a higher return than their benchmarks.
2. The mutual funds providing low returns to shareholders are persistent (they go on providing low returns).
3. The commissions, expenses and portfolio rotation have a lot of influence on the return of the funds.
4. It does not seem that "market timing" improves the return of the funds.

The authors conclude by advising investors to invest in funds with low commissions and expenses which replicate the indexes, and to avoid funds with "active management",[6] especially if they have not had a flawless past.

Gil-Bazo and Ruiz-Verdú (2007) have studied funds with active management and concluded that, curiously, the lower the performance of the fund is, the higher the commission.

Kraeussl and Sandelowsky (2007) showed that the predictive capacity of the ratings of mutual funds that were released by Morningstar is similar to the predictive capacity of a random prediction.

Friesen and Sapp (2007) researched the timing ability of investors and conclude that, between 1991 and 2004, the timing decisions of investors reduced their annual return by 1.56% on average.

Benchmarks Used in the Study

Our conclusions may depend on the benchmarks that are used. Are the benchmarks used in this study reasonable?

The benchmarks we used are rather conservative. **Table 9** summarizes the benchmarks that we used for the cases of stock mutual funds, short-term, fixed-income funds and long-term, fixed-income funds, and they are compared to other possible benchmarks.

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[6] Active management occurs when fund managers frequently sell securities and buy others, so that the portfolio composition changes. With the data that most Spanish mutual funds provide, it is impossible to know if active management determined any increase in the return to shareholders, although it did generate higher returns for the stock market departments that realized the purchase and sale of securities (they charged shareholders commissions). It seems reasonable that funds inform shareholders on the amount of purchases and sales they realized and on the amount of the commissions paid (although most of the funds do not). It would also be interesting if the funds provided the exact return they would have obtained if the portfolio had stayed the same: in this manner, we could know exactly the added value (or the decrease in value) generated by active management.

Spain's Stock Mutual Funds are compared to the overall index of the Madrid Stock Exchange (ITBM). After reading several affirmations from the advertisements of numerous mutual funds[7] (for example, optimal selection, the best investment advisors, best management, vision over the markets, advantageous for the shareholder, efficiency, objectivity, high return, demonstrated efficiency, value generation for shareholders, increase on value added, returns impossible to reach by individual investors, global management, deep market knowledge, 30 years of experience in fund management, opportunities identification, excellent management for your investment), we could expect the managers of Spanish stock funds to do more than just reproducing a market index. As we can see form Table 9, not very imaginative strategies, such as buying at the beginning of the year, companies with higher dividend yield (Top DIV) or companies with lower market price-to-book ratios (Top Book/P), provide slightly higher returns than the ITBM. On the other hand, the fact that Ibex 35 provided a lower return than the ITBM can be easily explained by acknowledging that, as usual, smaller companies perform better, on average, than big companies. Consequently, a portfolio made up of shares from medium companies, or an investment in the IBEX 35 but with a higher weight of small companies, will have higher gains than the ITBM.

Table 9

Benchmarks Used and Potential Benchmarks

		3 Years	5 Years	10 Years	16 Years
National Equity	*Benchmark:* ITBM (overall index of the Madrid Stock Exchange)	**24.5%**	**25.9%**	**13.7%**	**16.4%**
	IBEX 35 dividends	22.5%	24.1%	10.4%	15.1%
	IBEX 35 equally weighted	22.2%	25.7%	13.1%	16.4%
	Top 20 DIV weighted	26.3%	28.8%	20.6%	22.3%
	Top 25 DIV weighted	26.4%	26.0%	19.4%	22.0%
	Top 25 DIV equally weighted	21.5%	24.8%	20.2%	20.8%
	Top 30 DIV weighted	27.0%	26.3%	20.5%	22.6%
	Top 20 Book/P weighted	40.9%	36.5%	30.6%	30.8%
	Top 20 Book/P equally weighted	32.8%	32.8%	20.8%	25.1%
	Top 25 Book/P weighted	31.1%	30.5%	28.4%	28.2%
	Top 25 Book/P equally weighted	31.5%	31.6%	20.9%	23.8%
	Top 30 Book/P weighted	29.7%	30.4%	26.4%	27.5%
Short-term, fixed-income	***Benchmark:* AFI SPAIN GVT 1 DAY TREAS.BILL REPO**	**2.9%**	**2.6%**	**3.2%**	**5.5%**
	AFI SPAIN GVT 1 YEAR TREASURY BILL	2.7%	2.7%	3.4%	5.8%
	Roll-over 12-month bill (BDE)	3.2%	2.8%	3.3%	5.5%
Long-term, fixed-income	***Benchmark:* 50% 3 years y 50% 10 years**	**2.2%**	**3.7%**	**5.1%**	**8.5%**
	ES BENCHMARK 10 YEAR DS GOVT. INDEX	2.08%	4.26%	5.76%	9.51%

Short-term, fixed-income funds (with portfolios lasting under two years) were up against the return of one-day repos, even with other more advantageous options available.

Long-term, fixed-income products are compared to a portfolio distributed evenly between 3- and 10-year bonds (the comparison reveals that investing solely in the latter would be more profitable).

[7] See **Appendix 5.**

Fiscal Discrimination Favoring Mutual Funds and Going Against Independent Investors

If investors used their money the same way as a mutual fund would, they would obtain a different return because:

1. They could save all explicit commissions (and almost all hidden ones).
2. They would have additional expenses for holding and buying or selling securities, and
3. They would have to pay higher taxes!

Because of a preferential fiscal treatment favoring mutual funds, the Spanish government encourages this practice. Is this logical given the facts we analyzed? It seems otherwise. Nevertheless, the Spanish government could "stimulate" investment in some of the funds but not in an indiscriminative manner.

Conclusions

When investing in a mutual fund, one expects a higher return than one could obtain by managing the money oneself. Therefore, one is prepared to pay an annual commission, sometimes higher than 2%. However, the analyzed data shows that not all money managers deserve such high commissions.

In the past 10 years, mutual funds did not achieve sufficient results to cover the loss of value due to inflation.

In the past 10 and 16 years, the average return of the funds was below the return on an investment in state bonds at any term.

Despite these results, on December 31, 2007, 2,907 available funds were managing €238.699 billion for 8,264,240 shareholders.

Using rather conservative benchmarks, only 30 of the 935 10-year-history funds topped the yield benchmark. For example, from the 61 Spanish Equity Mutual Funds with more than 10 years of history, none of them outperformed the overall Index of the Madrid Stock Exchange (ITBM).

Looking back at the period 1992-2007, a yield of the funds on a par with the benchmark would have brought €180 billion instead of the €80 billion obtained. The total of fees and charges (explicit commissions), during the same period of time, reached €34 billion. The remaining €66 billion (100 – 34) is due to hidden commissions and investment decisions.

Some of the funds –although few– did obtain important gains for their shareholders and, therefore, offered a good justification for the commissions they charged.

Lastly, the global achievement of the funds offers no justification for such favorable fiscal conditions. However, the Spanish government could encourage investment in some of the funds but not in an indiscriminative manner.

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Appendix 1

Types of Funds and Benchmarks

NATIONAL

1) **FIAMM (Money Market Mutual Funds).** They were added to the following category: Short-term, Fixed-income.

2) **SHORT-TERM, FIXED-INCOME.** Average duration of the portfolio: less than 2 years. *Benchmark: AFI SPAIN GVT 1 DAY TREAS.BILL REPO.*

3) **LONG-TERM, FIXED-INCOME.** Average duration of the portfolio: over 2 years. *Benchmark: 50% ES BENCHMARK 3 YEAR DS GOVT. INDEX and 50% ES BENCHMARK 10 YEAR DS GOVT. INDEX.*

4) **MIXED, FIXED-INCOME.** Less than 30% of portfolio in shares. *Benchmark: 75% Long-term, Fixed-income and 25% ITBM (overall index of the Madrid Stock Exchange).*

5) **MIXED EQUITIES.** Between 30% and 75% of the portfolio in shares. A maximum of 30% in non-Euro currencies. *Benchmark: 30% Long-term, Fixed-income and 70% ITBM (overall index of the Madrid Stock Exchange).*

6) **SPANISH EQUITIES.** More than 75% of the assets in shares listed on Spanish stock markets, including Spanish securities listed on other markets. Investment in Spanish shares has to represent at least 90% of the equity portfolio. Maximum of 30% in non-Euro currencies. *Benchmark: ITBM.*

1), 2), 3) and 4): Assets in € currency (max. of 5% in non-Euro currencies).

1), 2) and 3): They include neither equities in their cash portfolio nor derivatives based on assets that are not fixed-income.

INTERNATIONAL

7) **FIAMM INTERNATIONAL.** They were added to the following category.

8) **INTERNATIONAL FIXED INCOME.** No equities in their cash portfolio nor derivatives based on assets that are not fixed-income. *Benchmark: US BENCHMARK 30 YEAR DS GOVT. INDEX – TRI.*

9) **INTERNATIONAL MIXED FIXED INCOME.** Less than 30% of portfolio in shares. *Benchmark: 75% INTERNACIONAL FIXED INCOME and 25% average of Equity: Euro, Europe, USA and Japan.*

7), 8) and 9): Assets in non-€ currency (max. of 5% in Euro currency).

10) **INTERNATIONAL MIXED EQUITIES.** Between 30% and 75% of the portfolio in shares. More than 30% in non-Euro currencies. *Benchmark: 30% INTERNATIONAL FIXED INCOME and 70% average of Equity: Euro, Europe, USA and Japan.*

11) **EURO EQUITIES.** More than 75% of the portfolio in shares. Spanish equities: Less than 90% of the equity portfolio. Less than 30% in non-Euro currencies. *Benchmark: 20% Eurostoxx 50 and 80% ITBM.*

12) **EUROPE INTERNATIONAL EQUITIES.** More than 75% of the portfolio in shares. European shares: More than 75% equity portfolio. More than 30% in non-€ currencies. *Benchmark: 50% Eurostoxx 50 and 50% FTSE 100.*

13) **USA INTERNATIONAL EQUITIES.** More than 75% of the portfolio in shares. U.S. shares: more than 75% equity portfolio. More than 30% in non-€ currencies. *Benchmark: S&P 500.*

14) **JAPAN INTERNATIONAL EQUITIES.** More than 75% of the portfolio in shares. Japanese shares: more than 75% equity portfolio. More than 30% in non-€ currencies. *Benchmark: Japan-DS.*

15) **EMERGING INTERNATIONAL EQUITIES.** More than 75% of the portfolio in shares. Emerging countries' shares: more than 75% equity portfolio. More than 30% in non-€ currencies. *Benchmark: MSCI Emerging Markets Index.*

16) **OTHER INTERNATIONAL EQUITIES.** More than 75% of the portfolio in shares. More than 30% in non-€ currencies. Different from previous categories. *Benchmark: Average of [11, 12, 13, 14 and 15].*

17) **GLOBAL FUNDS.** Funds whose investment policy is not precisely defined; they do not fit into any of the categories described. *Benchmark: Average of [11, 12, 13, 14 and 15].*

18) **GUARANTEED FIXED INCOME.** Fund with the guarantee of a third person (that can either favor the fund or the shareholders) and which can insure only a fixed return. *Benchmark: Average of AFI SPAIN GVT 1 YEAR TREASURY BILL and ES BENCHMARK 3 YEAR DS GOVT. INDEX.*

19) **GUARANTEED EQUITY FUNDS.** Fund with the guarantee of a third person (that can either favor the fund or the shareholders) and which can insure a return linked fully or partially to the performance of shares or currencies. *Benchmark: 70% AFI SPAIN GVT 1 YEAR TREASURY BILL and 30% IBEX 35.*

All funds are obliged to maintain an average monthly liquidity of 3% of the value of their asset holdings. This 3% could slightly change the quantitative results, but not the main conclusions of this paper.

Source: Inverco, last updated in January 2002

Appendix 2

Evolution of the Value of the Asset Holdings of the Number of Funds and the Number of Shareholders per Category, 1991-2007

Value of the asset holdings (€ billion)

		1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Fixed Income	Short-term	15.5	26.1	39.8	45.9	51.3	71.7	80.8	72.2	66.7	50.9	65.9	80.3	92.4	96.3	99.4	95.8	92,3
	Long-term	4.9	8	14.1	13.4	12.5	18.9	23.9	27.5	15.4	11.2	11.7	10.5	9.9	9.8	9.9	7	6,4
	Mixed	1.3	1.6	2.5	2.6	2.5	4.7	8.7	15.3	16.9	13.5	9.1	6.4	6.2	7.2	8	9.3	8,3
Equity	Mixed	0.42	0.6	1.8	1.9	1.6	2.7	7	11.5	13.4	12.2	9.9	6.9	6.7	6.4	6.7	6.8	6,3
	National	0.12	0.1	0.4	0.7	0.6	1.4	3.8	6.4	7.7	6.5	5.5	4	5.6	7.9	9.6	10.7	7,8
	Fixed Income	0.26	0.44	1.1	1.1	1	1.1	1.5	1.5	1.6	2.1	2.1	1.5	1.4	2.2	2.2	1.6	0,9
	F. Income Mixed	0.47	0.57	0.9	0.8	0.8	1.2	4.2	10.5	13.4	11.9	8.9	7.5	4.8	4	4.6	5.3	4,7
	Equity Mixed	0.05	0.06	0.15	0.28	0.26	0.7	2	3.3	4.5	5.6	4.5	2.4	2.5	3.1	3.5	3.6	2,7
	Variable Euro	0.1	0.09	0.27	0.47	0.45	1	2.7	4.3	6	7.7	5.3	3.2	3.5	3.5	5.1	6.5	7,7
Internat.	Var. Europe	0.01	0.02	0.1	0.1	0.1	0.1	0.9	2.9	3.7	5.3	3.8	2.3	2.7	3.1	5.1	6.7	5,7
	Variable USA	0	0.01	0.01	0	0	0.01	0.06	0.14	0.58	1.12	1.04	0.69	1.03	0.88	1.08	1.31	0,8
	Variable Japan	0	0	0.01	0.01	0.01	0.01	0.01	0.05	0.85	1.03	0.56	0.38	0.42	0.55	1.51	1.03	0,4
	Var. Emerging	0.01	0.01	0.03	0.02	0.01	0.02	0.25	0.24	0.32	0.51	0.39	0.25	0.31	0.54	1.3	1.6	2,1
	Variable Rest	0.01	0.05	0.13	0.16	0.12	0.17	1.1	2.3	7.7	9.8	6.5	3.9	4.2	4	4.6	5.4	4,5
	Globals	0.09	0.1	0.2	0.3	0.3	0.3	0.6	1.1	2.1	2.3	3	2.4	7.1	16.1	22.9	30.7	27,7
Guarant.	Fixed income					1.5	6.6	13.7	17.8	14.9	15	16.2	15.1	12.6	14.4	14.5	16.7	18,1
	Equity					0.2	1.9	11.3	26.4	29.7	26.8	25.2	23.0	36.7	39.6	45.9	44.1	42,2
TOTAL FUNDS		23,2	37.8	61.6	67.6	73.3	112	162	204	206	183	180	171	198	220	246	254	**238.7**

Number of funds		1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Fixed income	Short-term	137	181	218	234	249	298	352	376	400	398	371	372	411	398	357	373	**386**
	Long-term	66	89	101	105	118	136	157	165	166	173	162	151	155	154	153	147	144
	Mixed	48	58	65	77	85	99	123	153	181	194	177	167	166	154	142	142	136
Equity	Mixed	43	50	62	76	83	91	133	165	184	196	189	189	180	160	147	146	144
	National	23	26	30	46	43	52	74	88	91	93	102	102	111	114	119	120	122
	Fixed income	12	16	23	26	27	31	41	45	51	60	59	65	67	69	71	72	65
	F. income Mixed	11	18	22	26	28	32	38	53	75	84	83	90	97	83	72	75	76
	Equity Mixed	5	6	13	20	22	31	44	60	75	88	103	107	109	85	80	80	79
	Variable Euro	9	11	14	17	19	21	32	66	86	99	109	102	107	105	112	112	119
Internat.	Var. Europe	4	4	4	6	7	7	19	29	36	50	65	61	63	63	67	68	71
	Variable USA	1	1	1	1	1	2	6	9	23	37	48	50	49	44	41	41	43
	Variable Japan	1	1	2	2	2	2	2	7	16	29	29	28	27	23	24	26	25
	Var. Emerging	2	2	2	2	3	4	11	11	17	38	39	35	34	41	43	51	59
	Variable Rest	4	7	8	10	10	16	51	91	139	207	220	229	210	176	164	164	159
	Globals	8	10	14	15	16	20	40	57	82	104	164	131	180	258	295	351	**423**
Guarant.	Fixed income					27	82	167	188	184	195	209	210	215	226	230	272	262
	Equity					12	35	168	304	348	381	411	398	442	501	499	539	**594**
TOTAL FUNDS		374	480	579	663	752	959	1458	1867	2154	2426	2540	2487	2623	2654	2616	2779	**2.907**

Shareholders (thousand)		1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Fixed Income	Short-term	482	777	1,588	1,782	2,017	2,739	3,082	2,840	2,493	1,908	2,183	2,339	2,585	2,577	2,656	2,605	**2.450**
	Long-term	360	625	536	515	408	596	726	830	546	325	318	274	284	289	310	331	354
	Mixed	136	93	94	104	92	177	354	614	712	567	384	290	292	291	313	314	297
Equity	Mixed	50	41	87	110	82	113	302	503	565	558	463	384	361	327	291	257	260
	National	20	27	31	49	41	63	173	286	298	292	262	256	279	356	371	348	309
	Fixed Income	39	44	46	44	34	32	53	59	73	71	70	58	70	104	106	114	72
	F. Income Mixed	43	51	108	99	84	95	195	398	490	432	395	338	210	182	195	216	214
	Equity Mixed	3	4	10	17	14	25	67	126	158	249	233	201	176	143	131	110	91
	Variable Euro	2	3	23	40	33	49	124	187	210	313	292	252	248	223	258	290	300
Internat.	Var. Europe	2	2	4	9	7	10	49	164	124	229	191	188	180	195	244	260	259
	Variable USA	0	0	0	0	0	0	2	4	27	43	40	41	44	72	81	131	50
	Variable Japan	0	0	1	1	1	1	1	3	52	91	74	68	61	67	86	85	52
	Var. Emerging	1	1	2	2	2	2	19	24	24	43	37	34	32	46	78	112	157
	Variable Rest	2	3	13	17	12	13	54	129	363	732	660	626	577	509	425	397	303
	Globals	5	5	5	7	5	6	15	18	53	79	92	92	183	511	564	880	772
Guarant.	Fixed Income					105	291	538	660	566	548	597	550	430	494	544	584	578
	Equity					9	81	492	1,145	1,268	1,180	1,158	1,134	1,619	1,656	1,903	1,785	**1.747**
TOTAL FUNDS		1.145	1,677	2,548	2,794	2,944	4,290	6,243	7,984	8,012	7,655	7,449	7,127	7,632	8,041	8,555	8,820	8,264

Average value of holdings per fund (million €)

		1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Fixed Income	Short-term	113	144	183	196	206	240	230	192	167	128	178	216	225	242	279	257	239
	Long-term	74	90	140	127	106	139	152	167	93	64	72	70	64	63	65	48	44
	Mixed	27	28	39	33	29	47	71	100	93	70	51	38	37	47	56	65	61
Equity	Mixed	10	12	29	25	20	30	53	70	73	62	52	36	37	40	45	47	44
	National	5	5	14	14	15	26	51	73	84	70	54	39	50	69	81	89	64
Internat.	F. Income	21	27	49	42	37	35	36	34	32	35	36	24	20	32	31	23	14
	F. Inc. Mixed	43	31	42	31	27	37	109	198	179	142	107	84	49	49	63	71	62
	Equity Mixed	11	10	11	14	12	23	44	56	59	64	44	23	23	37	44	45	34
	Var. Euro	11	8	19	27	23	46	85	65	70	77	49	32	32	33	46	58	65
	Var. Europe	4	4	13	15	11	20	46	100	103	105	58	37	43	50	76	98	80
	Var. USA	5	8	6	4	3	6	10	15	25	30	22	14	21	20	26	32	19
	Var. Japan	1	1	4	4	4	3	3	8	53	36	19	14	16	24	63	40	18
	Var.Emerging	3	5	15	10	5	5	23	22	19	13	10	7	9	13	30	32	36
	Var. Rest	3	7	16	16	12	11	21	26	55	47	29	17	20	23	28	33	28
	Globals	11	13	16	19	17	16	15	20	25	22	18	18	39	62	78	88	66
Guarant.	Fixed Income					57	81	82	95	81	77	77	72	59	64	63	61	69
	Equity					18	53	67	87	85	70	61	58	83	79	92	82	71
TOTAL FUNDS		62	79	106	102	97	117	111	109	95	76	71	69	75	83	94	92	82

Average value of holdings per shareholder (thousand €)

		1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Fixed Income	Short-term	32	34	25	26	25	26	26	25	27	27	30	34	36	37	37	37	38
	Long-term	13	13	26	26	31	32	33	33	28	34	37	38	35	34	32	21	18
	Mixed	10	17	27	25	27	27	25	25	24	24	24	22	21	25	26	30	28
Equity	Mixed	8	14	21	17	20	24	23	23	24	22	21	18	19	20	23	27	24
	National	6	5	13	13	16	22	22	22	26	22	21	15	20	22	26	31	25
Internat.	Fixed Income	7	10	24	25	29	34	28	26	22	29	31	27	19	21	20	14	13
	F. Income Mixed	11	11	8	8	9	13	21	26	27	28	23	22	23	22	23	25	22
	Equity Mixed	20	14	15	17	19	28	29	27	28	23	19	12	14	22	27	33	30
	Variable Euro	41	28	11	12	14	19	22	23	29	25	18	13	14	16	20	23	26
	Var. Europe	9	7	12	10	11	15	18	18	30	23	20	12	15	16	21	26	22
	Variable USA	27	39	30	33	57	26	40	38	22	26	26	17	24	12	13	10	16
	Variable Japan	12	12	14	12	11	12	9	19	16	11	8	6	7	8	18	12	9
	Var. Emerging	7	7	14	8	7	10	13	10	13	12	10	7	9	12	16	14	13
	Variable Rest	5	16	10	10	10	13	19	18	21	13	10	6	7	8	11	14	15
	Globals	19	25	42	41	51	52	40	63	39	29	33	26	39	31	41	35	36
Guarant.	Fixed Income					15	23	25	27	26	27	27	27	29	29	27	29	31
	Equity					24	23	23	23	23	23	22	20	23	24	24	25	24
TOTAL FUNDS		20	23	24	24	25	26	26	26	26	24	24	24	26	27	29	29	29

Source: Inverco

Appendix 3

Calculation of Net Investment for each Year

Using the average return on every type of fund, every year, (R_t) and the every-year-value of asset holdings (P_t) provided by Inverco, we calculate Net Investment by shareholders (IN NET_t) with the equation: IN $NET_t = P_t - P_{t-1}\ (1+R_t)$. Net Investment is the difference between the contributions and withdrawals made by investors, assuming that all of them were realized on the last day of the year.

Net subscriptions (million €)		1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	3 Years	5 Years	10 Years	16 Years
Fixed Income	Short-term	15.529	8.916	11.254	3.250	1.584	16.857	5.735	-11.135	-6.372	-17.838	13.199	12.735	10.769	2.661	1.873	-5.639	-6.212	-9.978	3.452	-5.959	41.637
	Long-term	4.853	2.946	3.723	-293	-2.174	5.092	3.732	2.432	-11784	-4.887	84	-1.686	-823	-494	-43	-2.944	-697	-3.684	-5.001	-20.842	-7.816
	MIXED	1.296	221	671	15	-297	1.693	3.821	5.558	981	-3.367	-4.351	-2.357	-533	749	500	864	-1.192	172	388	-3.148	2.976
Equity	MIXED	422	170	1.049	208	-506	558	3.816	3.256	576	-304	-1.398	-1.311	-938	-801	-442	-703	-733	-1.878	-3.617	-2.798	2.497
	NATIONAL	123	22	205	286	-95	471	1.945	1.509	191	141	-376	-86	481	1.205	168	-1.948	-3.724	-5.504	-3.818	-2.439	395
Interna-tional	Fixed Income	256	167	545	10	-194	-23	249	2	47	356	2	-564	-201	825	-115	-524	-728	-1.367	-743	-900	-146
	F. Income MIXED	470	102	113	-118	-105	262	2.871	5.909	2.225	-1.296	-2.833	-1.025	-2.861	-890	328	609	-630	307	-3.444	-464	2.661
	VARIABLE MIXED	53	6	71	139	-47	356	1.129	1.173	544	1.464	-648	-1.238	-135	542	39	-105	-918	-984	-577	718	2.372
	VARIABLE EURO	102	-12	146	225	-77	342	1.463	967	253	2.036	-823	-319	-287	-280	880	475	1.004	2.359	1.792	3.906	5.993
	VARIABLE EUROPE	14	2	29	43	-22	35	712	1.824	-597	2.031	-461	-402	144	231	1.189	749	-919	1.019	1.394	3.789	4.588
	VARIABLE USA	5	3	-4	-2	-1	7	47	54	413	578	119	0	286	-151	92	188	-477	-197	-62	1.102	1.152
	VARIABLE JAPAN	1	0	6	2	-3	-3	1	48	762	442	-165	-39	-3	107	729	-375	-422	-68	36	1.084	1.087
	VARIABLE EMERGING	7	3	14	-7	-8	1	225	42	-31	240	-111	-30	-19	180	454	50	136	640	801	911	1.139
	VARIABLE REST	11	38	65	44	-58	2	848	**1.084**	**4.253**	**3.503**	-1.003	-169	-152	-310	-232	310	-877	-799	-1.261	6.407	7.346
	GLOBALS	90	41	65	71	-37	-64	240	411	775	348	865	-232	**4.589**	**8.779**	**5.883**	**6.932**	**-3.446**	9.369	22.737	24.904	25.220
Guarant.	Fixed Income		0	0	0	1.536	**4.820**	**6.444**	**3.109**	-2.676	-453	557	-1.768	-2.811	1.422	-175	2.048	977	2.850	1.461	230	13.030
	Equity		0	0	0	213	1.582	**9.162**	**12.749**	1.782	-2.571	-1.699	-2.357	**12.883**	1.495	4.716	-3.859	-2.947	-2.090	12.288	20.192	31.149
	TOTAL FUNDS	**23.234**	**12.625**	**17.953**	**3.874**	**-290**	**31.989**	**42.440**	**28.992**	**-8.657**	**-19.578**	**958**	**-845**	**20.388**	**15.269**	**15.845**	**-3.873**	**-21.805**	-9.833	25.824	26.694	135.285

Appendix 4

Fees and Expenses of Mutual Funds

Management commission: Commission paid out of fund assets to the fund's investment adviser. It can be established as a function of the value of the assets, of the returns or of both variables (there may be differences in the commissions according to the duration of the investment, etc.). There are maximum limits: 2.25% if applied to the value of the holdings, 18% if it depends on the return, and, if both variables are used, it can not be higher than 1.35% of the value of the holdings and 9% of the returns.

Deposit commission: A fee imposed on fund assets, in connection with the maintenance of the securities. Generally, this commission is not higher than an annual 2% of the value of the assets.

Subscription commission: Another type of fee that funds charge their shareholders as a percentage of the invested capital when subscribing for shares of the fund. It cannot be higher than 5% of the value of the subscribed shares. There may be differences depending on the duration of the investment, etc.

Refund Commission: A type of fee that funds impose on shareholders as a percentage of the capital that was refunded. It cannot be higher than 5% of the liquidity value of refunded shares. The conditions and amount of this type of load will depend on how long the investor holds his or her shares.

Discount favoring the fund: Sometimes the fund's investment adviser passes part of the subscription and refund commissions charged to the fund; it is called discount commission favoring the fund and it benefits all the fund's shareholders.

Total Fund Operating Expenses (TER, Total Expense Ratio): It represents a percentage of the total of a fund operating expenses from the beginning of the calendar year until the present date. Total expenses include management and deposit commissions, external services and other operating expenses. The less the percentage is, the higher the profit for the shareholders.

Source: CNMV

Appendix 5

Advertising Fragments Used by Some Mutual Funds (translated)

Asset management should be left to an **expert**. We have been considered one of the **best managers of equity funds** for years. Therefore, you can expect a high return for your money.

Our funds offer: 1. **Optimal selection**. We select the **best specialists** for all types of assets in order to ensure access to the **best investment advisers**. 2. **Active management**. Using this analysis and our vision of the markets, our team actively manages the portfolio. Dynamism and reduced cost are an important advantage for the shareholder in terms of **efficiency**.

Our investment style **has proven its efficiency**. **Active management** can **generate value** for the shareholders.

Our objective is to **efficiently** combine valued added management with personalized management. We propose the following **management style**: **active management** whose goal is to **protect the value of asset holdings** and strive for **long-term value**.

Mutual funds allow every individual access to the financial markets in an easy manner to allow them to **obtain returns that would be out of reach for independent investors**.

We offer the possibility of **global management**.

Our resources in analysis and asset management provide us with a **deep knowledge of the market**.

We offer more than 30 years of **management experience** in all types of assets in international markets, with team focused on **serving clients**.

Our analysts can **identify opportunities** that the market offers.

When you invest in our funds, you leave your money in the hands of managers capable of offering an **excellent management** of your investment.

Start saving now **without effort** and you will see how your money grows!

With our funds, you can expect **high-potential returns** and benefit from the lowest commissions on the market. To be more precise, you could save between 51% and 65% from the maximum legally allowed.

There is one certainty: the lower the commissions you pay, the more money in your pocket.

Our fund is managed by a team of professionals characterized by **talent and experience**.

Our funds allow you to make money easily, without having to lift a finger.

If you still have a few years left until retirement, we can provide you with **high-return funds** which would help you earn the money you need to add to your pension.

We offer **the most profitable funds** so that you can take advantage of your savings.

We **capitalize on the experience and advantages** acquired over time.

Our funds provide high returns for your savings with the best fiscal treatment.

Appendix 6

Press Clippings on the Evolution of Mutual Funds (translated)

In 2007:

The weighted average return in the past 12 months was 2.40%. The balance realized the last day of the year reflects the reality of the mutual funds as it is: moderate returns with a downward tendency caused by the second-semester crisis of subprime mortgages. Except for Emerging Equity, the other categories which made a profit were very moderate. Despite investment risks, the returns most of them obtained were lower than on a simple and safe term deposit...We hope 2008 will be more profitable.

In 2006:

In 2006 more than half of the mutual funds obtained a higher return than the market. Fifty-four percent of the mutual funds closed last year with real gains. Of the 2,585 funds available at the end of 2005 which remained on the market during 2006, 1,395 finished the year with a positive return, as their gains were higher than inflation.

The product with the highest return was the global fund CS Euroceánico Global (Credit Suisse) which gained 158.3%, followed by the Euro zone stock fund BK Pequeñas Compañías, with 60.8%. The first fund on the negative side was Córdoba Rural Rentabilidad Absoluta, with losses of 36.07%. Morgan Stanley Euro/Dolár 2005, a guaranteed fund, lost 17.2%, where as Morgan Stanley Dinerario lost 16.9% and Gaesco Japan had losses of 16.6%.

In 2005:

In 2005, mutual funds closed with a gain of 4.75%, a number that outperformed the inflation for the period – 3.8% - also the highest return of the past 6 years, according to Inverco. For the third consecutive year, all the families closed with positive values, although the ones with best results were those investing in emerging markets stock markets (54%). The next products with the highest returns were those investing in Japanese equity, given that between January and December 2005 they gained 39.8%.

On the other hand, money market funds (FIAMM) had the lowest gains in 2005, 1.17%, followed by short-term, fixed-income funds with 1.53%, and guaranteed equity funds with 1.87%.

Although equity funds had the highest returns, conservative products became the first money receptors, as €4.960 billion were invested in short-term, fixed-income funds, €3.738 billion in global funds and €2.984 billion in guaranteed equity funds.

In 1997:

In 1997, mutual funds were back on top of the list of products with highest gains. Their average profit was a lot higher than the return on bank deposits (around 5%). Direct equity investment itself generated a higher return (Madrid Stock Index gained 40% in 1997). However, equity purchase is, according to some experts, a riskier investment than buying shares in a mutual fund. Companies of mutual investment are managed by investment advisors who follow the markets on a daily basis and decide, according to circumstances, what and when to buy or sell.

Mutual funds invest the money in a lot of securities at the same time, offering small investors the opportunity to diversify. Moreover, fund managers consider 1998 stock market as being rather difficult.

Appendix 7

Comments by Readers on Previous Versions of this Paper (some translated)

I sincerely thought that good managers would outperform the index by 3 or 4% at least. If fund managers are incapable of generating higher returns than the indexes, then which is their role? Isn't it better to invest in shares directly?

I worked for four years in a securities agency as an agent and I said to myself never to invest in mutual funds or to recommend it to anybody. As an agent I used to earn commissions, while my clients lost money without explanation…

Any manager who could guarantee a better result than the index would now have been a long time in the Bahamas.

The Bestinver case deserves homage… and an analysis in order to learn.

I always had it clear: the winners are the funds and their investment advisers. It is better to buy shares directly rather than invest in a fund.

Funds with few transactions and investments in long-term (10 years) large companies' securities do have better results than the IBEX.

It is illogical that the AEAT maintain such favorable conditions for mutual funds given the complete uselessness of many fund managers. There is now the possibility of customers changing fund without being penalized but the independent investor still has no access to the favorable fiscal treatment that mutual funds enjoy.

If markets are efficient, the average expected return on a fund (given the volatility of the index) is the return on the index minus all expenses charged by the fund. The problem is which and how many should the costs of a fund be and deciding whether such costs do compensate for any other alternative to get to the index. Costs for an investor: fiscal, transaction costs, management, operating and distribution. Discussing this problem is similar to discussing whether tomatoes in the supermarket should have the same price as the one the farmer receives.

The fund's investment managers pass on to the bank distribution networks between the 80% and 95% of the commissions they charge.

The professional management of a fund should provide the shareholder with the following elements of value (that no other investments provide):

- A return that follows the index (no higher than that, as the theory of market efficiency postulates that statistically it is impossible to reach or promise) before the costs.
- Reasonable costs based on elements like: daily liquidity, diversification, operating control of the portfolio with its suitable reporting, implicit fiscal charges, an excellent network assessment to recommend which the most appropriate asset allocation, depending on the unique circumstances of each investor, security.

It seems that almost no fund investment adviser deserves his or her fees.

I only have two ideas: 1. Investment in the stock market is better than in a mutual fund. 2. Bestinver seems to be the only serious fund manager.

All this reminds me of the example of the monkey that obtained a higher return with its fund than the experts.

The "invention" of the benchmark was the way out for mediocre fund managers to justify themselves with an index. But I want to underline the role of a good manager. It is fundamental to trust in the professional profile of the person more than in the name of the fund or entity for which he or she is working.

Thank you so much, but I'm afraid that if you go on publishing such articles we are not going to be able to sell a fund for many years…

Few fund managers were able to outperform the indexes during large periods of time. The most famous one is Warren Buffet (Berkshire Hathaway). They usually buy undervalued shares and wait for the necessary period of time until the market recognizes their value. If, once they buy the shares, the value goes down they feel even happier as they then have the possibility of buying more at a lower price.

Does all this have anything to do with the Theory of Random Walk by Burton Malkiel?

The numbers speak for themselves while the fund managers are the only ones that obtained a return, outrageous, I would say. Then, why does the investor still invest in mutual funds? I personally think that a great majority of them are assessed by a fiscal assessor.

Banks are the main institutions that acknowledge to common citizens that the stock market offers high returns, but that their investment has to be managed by professionals. As they start losing, what makes clients go on is the promise of recuperation. The professionals always receive their commissions whether the fund won or lost.

Lucky me that in the past 5 years I kept my mother's money in non-managed index funds with low commissions!

An investor buying several shares randomly would have a higher return than the funds.

It would be interesting to compare the gains of the fund managers with that of their clients!

I personally got a return of 0.068% in three years in a guaranteed fund from XXX. Maybe sometimes the return on my savings will be enough to cover the loss of value due to inflation – this is my only target as a professional living off his insomnia and seeing money just as raw material.

The amount of explicit commissions was shocking and revealing… and the hidden commissions even more so.

It is strange that articles stating the contrary are sold on a daily basis. Unfortunately, it is a reality that does not affect solely the financial sector.

If you could only see how tired we are of keep explaining to our customers the matter of timing and the unfortunate fund-picking but they do not understand it. We offer numerous empirical proves but it does not work.

It is incredible how much we pay on management commissions when a passive management fund would provide a higher return in the long run (for a lower commission and a better performance).

I always kept my money in savings accounts: with small returns, but almost always inflation +1%, immediate availability, zero commissions and short-term. At the moment I enjoy the market circumstances, higher than 4%, always one-year Euribor minus 10-20 basic points.

Reading this document, I recall Nassim Taleb and his book "*Fooled by the Randomness*" or his more recent "*Black Swam*".

There is so much money unjustifiably spent on professional management of the portfolio without real results to explain it.

Something or somebody keeps changing the results leaving fund advisers used to offering explanations for their bad management, with no argument. I sincerely do not believe in "wrong decisions" and in the possibility of improving them, as they always favor a specific person and go against the shareholder.

I understood long ago the "mechanism" of mutual funds and gave up investing in them. Now I only invest in pension funds, conscious of giving part of my fiscal profits to the management agency.

I am a trader and I also manage the portfolio of the bank and…your daughter could definitely do it better!

The biggest problem is the lack of passive retail funds in Spain (with a vocation of "buy and hold") with passive-fund commissions (clearly under 0.5%). This is the main difference between the Spanish fund industry and the typically US/UK one, placing the Spanish industry in a worse statistical position.

Now that we have the ETFs, it's worth questioning the subscription fees charged by the great institutions.

I completely agree: stock funds have a lower return than market indexes, even if we look at the most conservative ones.

Lately, journalists seem to be on the side of fund managers in economic pages, which start to stink.

The funds trade a high volume of assets which allows them discounts in the sale and purchase commissions, that otherwise would be inaccessible to an independent investor.

The biggest problem with the funds is that they use politics ("stop loss", etc.) that require a great deal of transactions (which may generate more hidden commissions). This technique significantly decreases the return of a long-term investment.

An investor that was pressured in the 90s to sell his/her shares and to invest in a fund (for the fiscal benefits) and did not do so… is now laughing at the adviser who recommended it.

I invest in mutual funds that replicate market indexes because they have lower commissions and because I can have my own opinion on what an index is going to do.

There are many fund advisers who do not obtain any increase in value.

There are many different fund managers: some are good and many are mediocre or bad.

The Spanish market is very vulnerable to an US/UK invasion with a strategy of distribution acquisitions (or agreement with the large companies) and a lot of marketing.

The most important thing in Spain is to channel family savings into investment. The percentage of investment in equity in Spain is a lot lower than the European or US/UK average.

I think that most investors invest in mutual funds because they look for a higher return than inflation and bonds…and they don't really care about outperforming the benchmark. As your analysis well shows, an independent investor could have outperformed the return on the funds…but maybe the investors think they could use this loss of time, effort and dedication in a better way … work, holidays, books, sports, rest, etc…?

I met so many clients who were upset because of a negative return on the fund or because of an excessively low return…for not being able to get a bigger portion of a good start.

Fiscal treatment should be the same for direct investment and for investment through mutual funds. The only difference is the degree of complexity of the fund management but the investment philosophy is the same.

I am a small investor in Vanguard funds (indexed, minimum commissions and which do not require any concern regarding the quality of the manager or the small print) and in Bestinver. This saves me from feeling like a fool when I read the front pages and the rankings of economic journals.

My first savings went to mutual funds. I got a low return in one of them and lost in the other one. First disappointment - I thought foreigners could do it better. I was recommended some experts (Growth portfolio) and I still have losses after 5 years. Of course, they charged commissions: in the first year, they would take 4%, in the second, 3%... I no longer buy funds. My recommendation: buy in the stock market using your own criteria and do the fund yourself. You will make more money, have fun and it will be only your own fault if you go bankrupt.

Almost all funds should return commissions: I do not need anybody else in order to make less money than with a fund indexed to the Madrid Stock Exchange.

The most important matter is to have a good investment adviser who could make you enter a fund at the right moment, leave it when it is no longer appropriate and enter the same fund or another one when things are back on track.

If one buys a fund and remains inactive over the years, then the return will not be optimized.

If we calculated the average of the funds and take into consideration the few good ones and the large group of mediocre and bad then the return we would get would be the one from your paper.

I am going to buy Treasury bills, now!

The truth is that I do not really know whether it is better to have a lot of money invested in funds at such low returns, or, as in my case, to have the right amount to live well, without expecting high returns but, at least, not having to feel "cheated"…

Mutual funds are just an old wives' tale…the only people who make money with them are the banks.

This shows the persistency of alpha is a tall story. That is why fund selection (or management, actually) is so difficult.

Hedge funds are going to be the next fraud, as they are abusive in commissions. And the worst thing is that the fiscal regime is very favorable for the funds; one can move from a fund to another without paying taxes but one cannot sell Iberdrola and buy Telefónica in the same way. With money and fixed-income funds the difference is based on commissions. Cheap funds do it well, but there are others which are very, very expensive.

Our organization does numerous analyses that, unfortunately, reach the same conclusion.