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ICI to Gensler: Look at the Facts

Washington, DC, September 14, 2023—The Investment Company Institute (ICI) President and CEO Eric J. Pan issued the following statement regarding Securities and Exchange Commission (SEC) Chair Gary Gensler's testimony to the U.S. Senate Banking Committee this week, in which Gensler repeated his unsupported assertion that mutual funds requested a rescue during the market volatility the U.S. experienced in March 2020, at the onset of the coronavirus crisis:

> *"In testimony before the Senate Banking Committee, Chair Gensler repeated his assertion of alleged phone calls made by the mutual fund industry to the SEC in March 2020 asking for rescue, stating that these phone calls justify the SEC's recent mutual fund swing pricing and liquidity risk management rulemaking. As the organization representing the fund industry, we have no knowledge of any such panicked calls having been made in March 2020.*
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> *"We are aware of information-sharing conversations by the industry with regulators at that time, as there should be during any period of market stress. We hope Chair Gensler is not suggesting that the industry should have withheld timely information on market conditions from the SEC out of concern that these conversations would later be mischaracterized to support future rulemaking.*
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> *"Unsubstantiated assertions should not be a basis for rulemaking."*

Background

In response to a question from U.S. Senator Robert Menendez, Chair Gensler claims that the SEC and Federal Reserve received calls from the industry asking for a bond mutual fund rescue "because there was such rapid redemptions and a fear of those rapid redemptions." Gensler explains that these calls are the reason he has proposed a sweeping and costly mutual fund swing pricing and liquidity risk management rulemaking – a proposal which has received significant bipartisan criticism in Congress, as well as from ICI.

Gensler further claims that his rule is needed to address the "dilution" effect experienced by fund investors in March 2020. But there was not a significant effect in March 2020, as shown by ICI's empirical analysis of dilution during that period.

- ICI research found that in March 2020, estimated dilution remained negligible, especially compared to the negative market returns arising from the rapid deterioration in global macroeconomic conditions.
- Moreover, as a regulatory hypothesis for future rulemakings, ICI research found that dilution is far too small to motivate redemptions, and pales in comparison the returns enjoyed by long-term investors.
  - Dilution occurs when fund shareholders redeem and the transaction costs of meeting those redemptions—such as bid-ask spreads or the market impact costs from the fund having to sell portfolio securities—are borne by non-redeeming shareholders as a reduction in the fund's returns.
  - ICI research estimates that dilution for US high-yield bond mutual funds averaged 3 to 6 basis points per annum from 2009 to 2022. Although not zero, these estimates give a sense of how small dilution is likely to be on a daily basis, and even more so compared to the large daily returns on such funds during periods of stress.

ICI has done significant research into the experience of bond mutual funds in March 2020, including:

- ICI's survey of bond mutual funds' daily activities in March 2020 shows that bond mutual funds sold, on net, far fewer Treasury notes and bonds in March 2020 than originally estimated by policymakers—only $101 billion.
- Our research shows that the Treasury market became significantly dislocated several days before bond mutual funds began selling Treasury bonds in any appreciable magnitude. Moreover, bond mutual funds' small share of Treasury trading volumes indicates their net sales must have had only a minor impact on the Treasury market.
- An ICI study shows that bond mutual funds' activities during March 2020 had little impact on the investment grade corporate bond market. Core bond mutual funds, on net, sold only $8 billion of their $780 billion in holdings of investment grade corporate

bonds in the first three weeks of March 2020.

For those interested in the money market fund (MMF) experience in March 2020, which is distinct from the experience of bond mutual funds, click here to read ICI's analysis of MMFs' weekly liquid assets.
