

ICI VIEWPOINTS

JULY 13, 2021

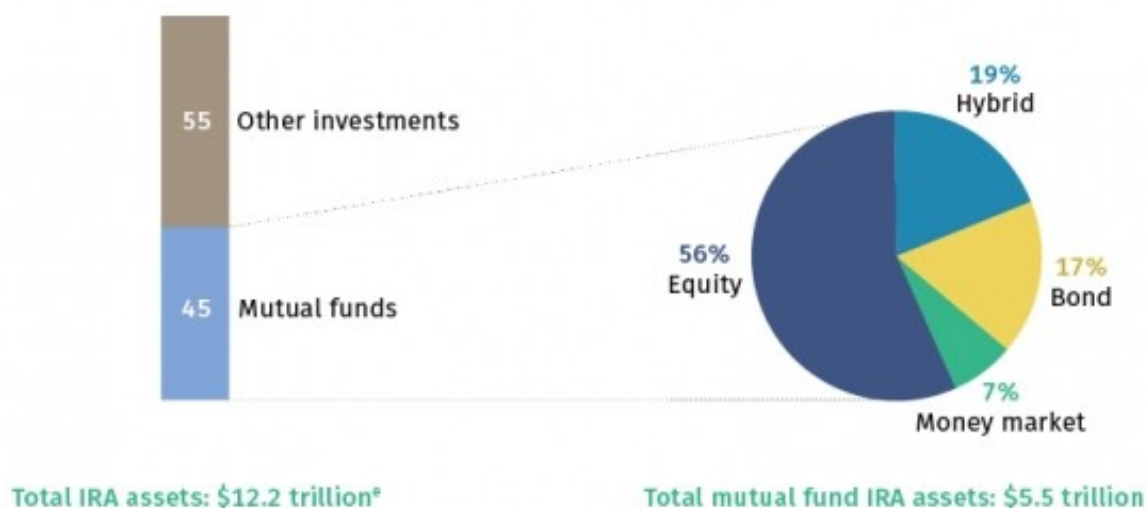
IRA Investors Are Concentrated in Lower-Cost Mutual Funds

By James Duvall

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Individual retirement accounts (IRAs) represent the largest share of assets in the [US retirement market](#), with assets totaling \$12.2 trillion at year-end 2020 (Figure 1). Forty-five percent of this total is held in mutual funds, with IRA mutual fund investors primarily invested in equity funds.

Figure 1
45 Percent of IRA Assets Are Invested in Mutual Funds
Percentage of assets, year-end 2020



^e Data are estimated

Sources: Investment Company Institute and Federal Reserve Board

[Like other mutual fund investors](#), IRA mutual fund investors incur expenses and fees that cover the costs of investing in mutual funds. ICI uses asset-weighted average expense ratios to measure the expense ratios that mutual fund investors actually incur for investing in mutual funds. A fund's expense ratio is the fund's total annual expenses expressed as a percentage of its total net assets. In 2020,

the trends for the average expense ratios for IRA mutual fund investors included:

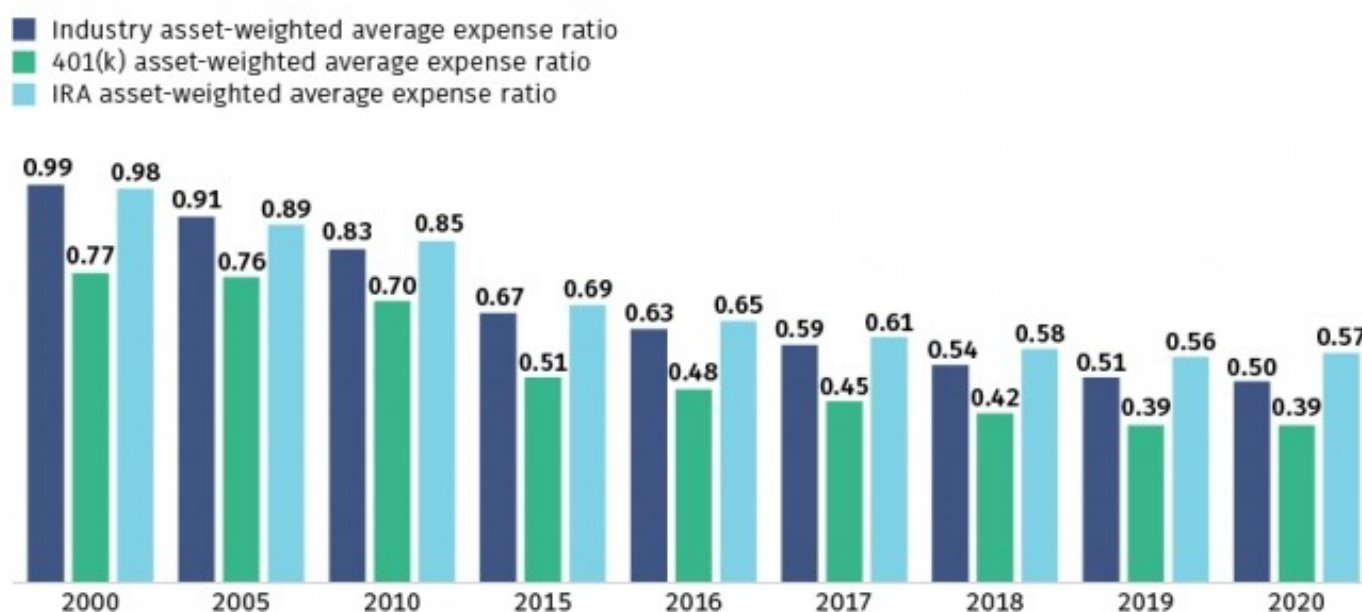
- average expense ratios paid by bond and hybrid IRA mutual fund investors continued to trend downward in 2020,
- IRA mutual fund investors paid average expense ratios similar to those paid by all mutual fund investors (i.e., industrywide), and
- IRA investors, like those in 401(k) plans and industrywide, continued to concentrate their assets in lower-cost mutual funds.

And although 401(k) plan investors pay lower average expense ratios when compared with investors industrywide and in IRAs, the differences can be explained, in part, by plan economies of scale, plan sponsor decisions to cover a portion of 401(k) plan costs, and use of financial professionals by IRA and retail investors.

Average Expense Ratios Paid by IRA Mutual Fund Investors

IRA equity mutual fund assets (including both active and index investment styles) represented 56 percent of IRA mutual fund assets at year-end 2020. The average expense ratio paid by equity mutual fund investors in IRAs increased 1 basis point in 2020, from 0.56 percent to 0.57 percent, but is far below its level of 0.98 percent in 2000 (Figure 2).

Figure 2
Equity Mutual Fund Expense Ratios
Percent



Note: Equity mutual funds in this figure encompass diverse investment styles (e.g., active and index); a range of general investment types (such as growth, sector, alternative strategies, value, and blend); and a variety of arrangements for shareholder services, recordkeeping, or distribution charges (known as 12b-1 fees). Data exclude mutual funds available as investment choices in variable annuities.

Sources: Investment Company Institute, Lipper, and Morningstar

IRA bond mutual fund assets (including both active and index investment styles) were 17 percent of IRA mutual fund assets at year-end 2020. Average expense ratios for bond mutual funds held by IRA investors have decreased sharply over the past five years and are down 54 percent from their level in 2000. The average expense ratio paid by bond mutual fund investors in IRAs fell to 0.39 percent in 2020, down from 0.41 percent in 2019 and 0.85 percent in 2000 (Figure 3).

Figure 3
Bond Mutual Fund Expense Ratios
Percent

■ Industry asset-weighted average expense ratio
■ 401(k) asset-weighted average expense ratio
■ IRA asset-weighted average expense ratio



Note: Fund investment categories include active and index investment styles. Data exclude mutual funds available as investment choices in variable annuities and tax-exempt mutual funds.

Sources: Investment Company Institute, Lipper, and Morningstar

Nineteen percent of IRA mutual fund assets were invested in hybrid mutual funds (including both active and index investment styles) at year-end 2020. Average expense ratios for hybrid mutual funds held by IRA investors have fallen for 11 consecutive years and are down 38 percent from their level in 2000. The average expense ratio paid by hybrid mutual fund investors in IRAs fell to 0.55 percent in 2020, down from 0.57 percent in 2019 and 0.89 percent in 2000 (Figure 4).

Figure 4
Hybrid Mutual Fund Expense Ratios
Percent

■ Industry asset-weighted average expense ratio
■ 401(k) asset-weighted average expense ratio
■ IRA asset-weighted average expense ratio



Note: Fund investment categories include active and index investment styles. Data exclude mutual funds available as investment choices in variable annuities.

Sources: Investment Company Institute, Lipper, and Morningstar

A Comparison with 401(k) Mutual Fund Investors

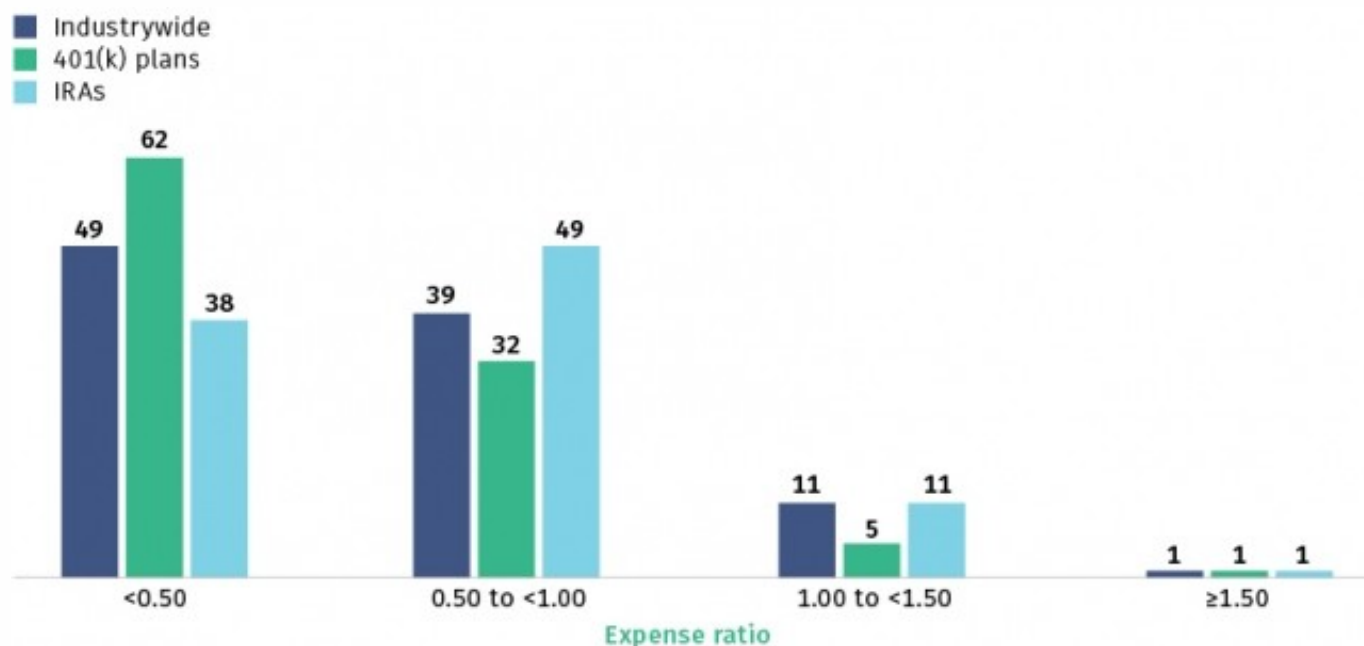
The data show that [401\(k\) investors, on average, incur lower expense ratios](#) in their mutual fund holdings than IRA mutual fund investors. One reason for this is economies of scale, as many employer plans aggregate the savings of hundreds or thousands of workers, and often carry large average account balances, which are more cost-effective to service. In addition, employers that sponsor 401(k) plans may defray some of the costs of running the plan, enabling the sponsor to select lower-cost funds (or fund share classes) for the plan.

Another difference: IRA investors often pay for the [assistance of a financial professional when investing](#), and sometimes cover the cost of this service by investing in a fund (or fund share class) that has a 12b-1 fee. This fee, which the fund collects and passes to the financial professional assisting the IRA investor, is included in the fund's expense ratio. 401(k) plan participants have generally had more limited access to professional financial advice, so 401(k) plans commonly select funds (or fund share classes) that provide no compensation for financial professionals—which partly explains their somewhat lower expense ratios.

IRA Investors Concentrate Their Assets in Lower-Cost Funds

Like mutual fund assets in 401(k) plans and across the industry, IRA mutual fund assets tend to be concentrated in lower-cost mutual funds. At year-end 2020, 87 percent of equity mutual fund assets (including both active and index investment styles) held by IRAs were invested in mutual funds with expense ratios of less than 1.00 percent, with 38 percent invested in equity mutual funds with expense ratios of less than 0.50 percent (Figure 5).

Figure 5
Equity Mutual Fund Assets Held in IRAs Are Concentrated in Lower-Cost Funds
Percentage of industrywide, 401(k) plan, and IRA equity mutual fund assets, 2020



Note: Equity mutual funds in this figure encompass diverse investment styles (e.g., active and index); a range of general investment types (such as growth, sector, alternative strategies, value, and blend); and a variety of arrangements for shareholder services, recordkeeping, or distribution charges (known as 12b-1 fees). Data exclude mutual funds available as investment choices in variable annuities.

Sources: Investment Company Institute and Morningstar

ICI Methodology

ICI evaluates fee trends using asset-weighted averages to summarize the expenses that shareholders actually pay through funds. To compute the average, ICI weights each fund's expense ratio by that fund's end-of-year total net assets. Simple averages (counting each fund's expense ratio equally) overstate the impact of the expenses of funds in which investors hold few dollars.

The fund investment categories used in this report are broad and encompass diverse investment styles (e.g., active and index); a

range of general investment types (e.g., equity, bond, and hybrid funds); and a variety of arrangements for shareholder services, recordkeeping, or distribution charges (known as 12b-1 fees). This material is intended to provide general information on fees incurred by investors through funds and insight into average fees across the marketplace. It is not intended for benchmarking fees and expenses incurred by a particular investor or charged by a particular fund or other investment product.

Find data on all figures in this report, including additional data on expense ratios between 2000 and 2020, [here](#). For more information about IRAs, visit our [Individual Retirement Account Resource Center](#).

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