

Falling Costs, Both Sides of the Pond

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Policymakers and commentators are paying more attention than ever to UCITS ongoing charges—particularly how they compare to US charges. Though this heightened scrutiny is understandable, it has led to two common misperceptions. First, that declines in UCITS ongoing charges are “too small.” Second, that UCITS ongoing charges are “too high.” ICI analysis on UCITS fees sets the record straight.

Let’s take the first misunderstanding: declines in UCITS ongoing charges are “too small.” ICI analysis shows that recent declines in UCITS ongoing charges are actually similar to those for US mutual funds. Between 2014 and 2019, the average rate of decline for equity UCITS ongoing charges was 4.2 basis points per year, compared with 3.8 basis points for equity US mutual funds. For fixed income funds, the average rate of decline for UCITS ongoing charges was 3.3 basis points per year, compared with 2.5 basis points for US mutual funds.

Meaningful Declines

Some say that these declines are too small and have no substantial impact. But they’re missing the fact that these “small” changes add up to meaningful declines over time. For example, from 1996 to 2019, the asset-weighted expense ratio of equity US mutual funds declined a total of 51 percent, even though the average rate of decline was only 2.3 basis points per year. Data on ongoing charges for UCITS do not have such a long history, but just from 2013 to 2019, UCITS ongoing charges have fallen significantly—17 percent for equity UCITS and 20 percent for fixed-income UCITS. As the UCITS industry continues to mature, these “small” changes in ongoing charges are likely to continue and result in a substantial cumulative decrease.

What about the second misunderstanding, that UCITS ongoing charges are “too high”? Although average ongoing charges for UCITS are higher than expense ratios for US mutual funds, some key reasons account for the difference, including:

- Different models for payments of distribution and advice. US fund investors have increasingly chosen to pay for distribution and advice out of pocket rather than through fund fees and expenses. At year-end 2019, 72 percent of US mutual funds were in “no-load” share classes, where any payments to financial professionals largely occur outside of the fund. By contrast, at least half of the assets in retail UCITS share classes were in bundled share classes that included these payments.
- Economies of scale. Some fund costs are relatively fixed and these costs contribute less to the ongoing charge for a larger fund than for a smaller fund. US mutual funds, on average, are substantially larger than UCITS funds. At year-end 2019, US mutual funds had an average of €2.1 billion in assets compared with €309 million for UCITS.

The US mutual fund and UCITS markets are different, and policymakers must consider each market’s unique aspects when comparing ongoing charges between them. Most importantly, UCITS ongoing charges have steadily decreased since 2013 as the distribution and regulatory landscape has evolved, the UCITS industry has grown, and UCITS investors have gravitated toward lower-cost products.