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Fund investors begin slowly embracing US stocks

By MARK JEWELL
AP Personal Finance Writer

BOSTON (AP) -- It appears investors are beginning to get comfortable with risk again. Not only are they pulling money out of bond mutual funds at the fastest pace in two years, but they're slowly starting to embrace stocks again.

The shift in sentiment comes as positive economic news and robust corporate earnings lift stocks, which have risen 20 percent since the start of September.

Prices of bonds, typically less risky than stocks, are heading in the opposite direction. A broad measure of the bond market, the Barclays Capital U.S. Aggregate Bond index, is down nearly 3 percent since early November. This reflects fears about rising interest rates, which effectively lower bond returns.

"You've almost got a one-two punch, with stocks up, and the bond market taking a pretty big hit," says Ron Saba, director of stock research with Horizon Investments, a Charlotte, N.C.-based investment adviser for \$3 billion in assets. "So now you start to see psychology take over. Investors say, 'I want to invest where I'm making money.'"

For the last few months, there's been a disconnect between the market's gains and investor behavior. Investors have been withdrawing more money from U.S. stock mutual funds than they've been adding. There hasn't been a positive weekly net flow of cash since late April, according to the Investment Company Institute.

That has finally changed. The fund industry organization reported Wednesday that investors added a net \$335 million into U.S. stock funds during the week ended Dec. 21.

Although that's a small amount - stock funds hold more than \$5 trillion in assets - the switch to positive flow comes after the pace of U.S. stock fund withdrawals has recently slowed.

Meanwhile, more than \$20 billion has been pulled out of bond funds since mid-November, with the weekly outflow in mid-December marking the biggest in more than two years.

"At the end of the year, a lot of investors have been looking at what stocks have been doing and asking, 'What am I sitting in bonds for?'" says Cleve Rueckert, a strategist with Birinyi Associates, a stock research and money management firm in Westport, Conn.

The Standard & Poor's 500 stock index is up 15 percent this year including dividends, more than twice the return of the comparable bond index.

The advantage for stocks was even bigger in 2009, when markets began recovering from a financial crisis that soured many investors.

That has led to a massive shift into the relative safe haven of bonds. Investors have added a net \$640 billion to bond funds since January 2009, according to ICI data. When investors have sought the higher potential returns of stocks, their search has taken them overseas. U.S. stock funds have consistently seen money flow out, while funds buying stocks of foreign companies have taken money in.

But positive sentiment is coming home, especially with many recognizable U.S. stocks faring well. Year-to-date, Apple Inc. is up more than 50 percent. Shares of Netflix Inc. have more than tripled in value, and Priceline.com has nearly doubled.

Investing pros also are also turning more positive. At least three surveys of money managers this month show growing confidence.

Some of the frequently cited reasons:

- Stocks remain cheap by the most widely used measures. The price-to-earnings ratio for Standard & Poor's 500 index stocks was 15.75 on Thursday, based on earnings from the trailing 12 months, according to Rueckert. Over the past two decades, the average has been around 23.

- Volatility has eased. The rapid swings in the the stock market have turned off many investors. A year or two ago, daily movements in the Dow of more than a full percentage point were the norm. But that's tapered off, and the Chicago Board of Options Exchange's Volatility Index is running at its lowest level in

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eight months. The index, known as Wall Street's fear gauge, is now roughly a third of where it stood during the financial crisis in 2008.

- Most economic indicators are positive. The deal between Congress and President Obama to extend Bush era tax cuts is expected to give the economy a short-term boost. Despite continuing housing market troubles, most data suggest the economic recovery is regaining momentum after stalling over the summer. For example, the government reported Thursday that the number of people applying for unemployment benefits fell to its lowest point in nearly two and a half years.

Those are the key reasons why Harry Rowen, CEO of Starmont Asset Management, has gradually been increasing the stock component of the more than \$100 million his San Francisco-based firm manages for wealthy individual investors.

Now that total is about half in stocks, half in bonds. Rowen expects to increase the stock component to 60 to 70 percent in coming months, anticipating stocks will continue rising after posting what could be the market's best December showing in 20 years.

But Rowen is moving slowly and cautiously.

"My clients are still very skittish - most of them have a good deal of money already, and they like to preserve it," he says. "So our moves back into stocks" he says, "are coming in small steps."

Questions? E-mail [investorinsight\(at\)ap.org](mailto:investorinsight(at)ap.org).

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