

Shareholders Likely to Misinterpret Bond Fund Risk Ratings, October 1997

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Washington, DC, October 31, 1997 - Mutual fund shareholders are likely to rely on but misinterpret the risk ratings for bond mutual funds that have been proposed by certain rating agencies, according to the final results of a [survey](#) released today by the Investment Company Institute. The survey was undertaken to determine whether those bond fund risk ratings would be used and understood by individuals who invest in mutual funds.

Although NASD Regulation, Inc. currently prohibits the use of risk ratings in bond fund sales literature, several firms that propose to sell risk ratings have petitioned the NASDR to end the prohibition.

The survey questioned a randomly selected sample of more than 600 fund owners who had examined bond fund sales literature containing simulated risk ratings for an established U.S. Treasury bond mutual fund. The final results confirm the preliminary findings, which were released in mid-September. Among the key findings:

- Mutual fund shareholders, including those with a minimal understanding of bond fund investing, are attracted to risk ratings. If ratings were available, more than half of those surveyed (54 percent) would rely on them when considering investing in a bond fund.
- Nearly 80 percent of participants said they would be very or somewhat confident in using risk ratings.
- Mutual fund shareholders misinterpret bond fund risk ratings. Sixty percent of respondents failed to recognize that risk ratings provide information about interest rate risk.
- Many respondents indicated that they would rely on ratings more than on the risk assessment measure they currently use. This suggests that fewer investors might turn to a narrative disclosure of investment risk if the use of risk ratings were permitted.
- The vast majority of shareholders surveyed hold erroneous beliefs about the workings of bond fund risk rating systems. The majority believe that such ratings would be: (1) available for every bond fund (70 percent of respondents); (2) available even if the fund was rated high risk (83 percent); (3) computed using a consistent method (81 percent); (4) issued by an entity regulated by a government agency (61 percent); and (5) subject to review by independent third parties (74 percent). None of those suppositions is true of bond fund risk ratings as [currently proposed](#).

The Investment Company Institute is the national association of the American investment company industry. Its membership includes 6,661 open-end investment companies ("mutual funds"), 443 closed-end investment companies, and 10 sponsors of unit investment trusts. Its mutual fund members have assets of about \$4.160 trillion, accounting for approximately 95% of total industry assets, and have over 59 million individual shareholders.