

(A)t the end of their fiscal year 1964, despite substantial net capital inflow between 1958 and 1964, half of the 10 (largest) funds had reduced the number of common stock issues held by them from the number held at their fiscal yearends 1958. The largest fund, Investors Mutual, Inc., reduced its holdings by 37 percent from 208 to 131 issues. The largest reduction was 44 percent—from 165 to 92—for Fidelity Fund, Inc.”¹⁶

Based on fund activity *alone* we are also told that the ability to both buy and sell is hampered when size reaches a given level and a limited investment policy is pursued. Examples, though dated and therefore understated, were not lacking in the report. A fund manager for a complex authorized in September 1962 the purchase of 443,000 shares of a company for two funds under its management. By March 1963 less than half the purchase order of one fund and less than 10 percent of that of the other had been filled. During this period the price per share had increased from \$40 to \$48.¹⁷

But perhaps even more alarming is an example given on the sell side. An advisor for one of the largest funds spotted unfavorable factors affecting one of their portfolio securities. A decision was made to sell 220,000 shares when the market stood at \$57 a share. (In this regard it should be noted that the report does not indicate whether the 220,000 constituted all that the fund possessed of the questioned issue.) However, before the fund's "selling program" could be effected the price per share had dropped to the midforties.¹⁸

If mutual funds were pension funds, there might be less reason to be disturbed. If mutual funds could buy for long-term holding, there might even be benefit in the rapid absorption of the floating supply of stock. But mutual funds are not pension funds. They are subject to the demands that are imposed by their own internal and industry structure.

The mutual fund industry is concentrated and dominated by billion-dollar enterprises. The structure of a mutual fund generally requires it constantly to sell fund shares in order to meet redemptions. In turn, the sales effort in no small way is financed by the give-up device resulting from brokerage. Add to this the need to sustain a given distribution "policy" and we can better understand the pressure on mutual funds to trade. They, unlike pensions funds, cannot anticipate with any precision the demands that will be made upon the entity.¹⁹

Now couple these facts with that of an institutionalized market. What is the meaning for mutual funds? How important to fund shareholders, to free securities markets, and to relations with portfolio corporations is the impairment of portfolio mobility and flexibility? The Commission stated: "Should the growth of the largest funds and fund complexes continue these funds might soon reach the point—relative to the size and conditions of the markets and the economy—where their portfolio mobility would be so seriously impaired as to affect gravely the interests of their shareholders. It is indeed possible that the future investment experience of the largest funds, even if their sizes were to continue near the present levels achieved only recently, might be so affected. This is underscored by the fact that other institutional investors, pension funds in particular, have also enjoyed phenomenal growth and are contributing to the growing problems of portfolio mobility. For these reasons, questions pertaining to large fund size and to the need for maximum size limitations on individual funds and fund complexes must be reexamined periodically in the context of the changing conditions in the securities markets and the economy.”²⁰

IV

The difficulty with the Commission's position is that in a very real sense the future which it fears already is here. Taking the facts as given, without any thorough analysis of institutional behavior, we know that *because of size* mutual funds now cannot exercise their best judgment. They can neither buy nor sell

¹⁶ Id. at 295-96. The Dreyfus Fund, Inc. and National Investors Corp. were identified in the Wharton Report as having more than 40 holdings of one percent or more of the outstanding voting stock of portfolio companies on September 30, 1958. Id. at 295. See also, Report at 255.

¹⁷ Id. at 256.

¹⁸ Ibid.

¹⁹ With the development of the fund of funds how much more difficult is the position of mutual funds. The threat of massive redemptions is not one to be taken lightly. Id. at 299.

²⁰ Id. at 263.