

Box 4

IMPACT OF TRANSACTIONS AND VALUATION EFFECTS ON THE VALUE OF EURO AREA INVESTMENT FUNDS

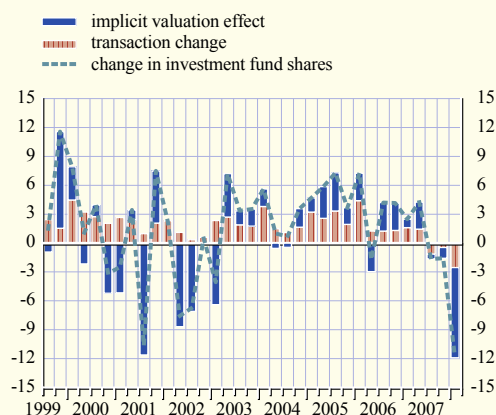
In the first quarter of 2008 the value of the total assets/liabilities of euro area investment funds (excluding money market funds) fell by 9.9% compared with the previous year. Such strong declines in asset values have been observed on previous occasions (such as the period of financial uncertainty between 2001 and 2003), and their assessment depends on the extent to which they arise from changes in transactions or valuation changes. This assessment can now be enhanced using newly available data on transactions.

The ECB has published euro area investment fund statistics since January 2003. While until mid-2008 the published data consisted only of outstanding amounts, in its data release on 10 July 2008 for the first quarter of 2008, the ECB published for the first time data on transactions involving shares issued by investment funds.¹ These transactions comprise investors' total net inflows into investment funds, which are calculated by adding investors' net purchases of investment fund shares to the income received by investment funds and subtracting dividends paid by funds. These data cannot yet be broken down by type of investment fund. Starting in the third quarter of 1999, they complement the data on outstanding amounts, which date back to the fourth quarter of 1998.

Chart A shows how quarter-on-quarter changes in the value of investment funds' assets are broken down into changes in transactions and valuation changes. The latter mostly reflect changes in asset prices, but also include the impact of exchange rate movements and incidental statistical reclassifications. It appears that the decline in the value of funds' assets in the first quarter of 2008 was due mostly to negative valuation effects, with only a small amount attributable to reduced transactions. This seems to hold also for other declines in asset values observed since the start of Stage

Chart A Contributions to changes in investment fund shares

(quarter-on-quarter percentage changes; percentage points)

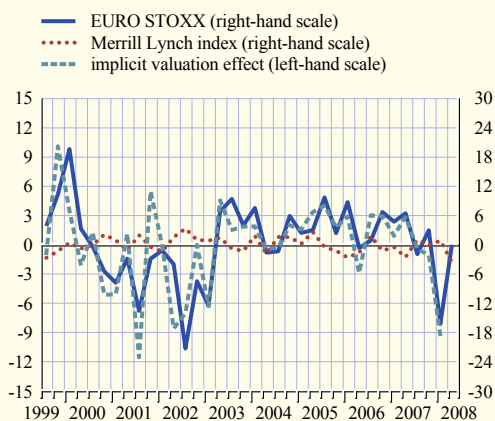


Note: Data are available up to the first quarter of 2008.

¹ These new transaction data allow a more elaborate analysis of investment fund shares, which currently represent around 94% of total investment fund liabilities. The new transaction data can be found in the Statistical Data Warehouse (<http://sdw.ecb.europa.eu>) on the ECB's website.

Chart B Valuation effects, stock market prices and bond prices

(percentages)



Sources: Bloomberg, ECB and Merrill Lynch.

Notes: "EURO STOXX" refers to the EURO STOXX stock market price index. "Merrill Lynch index" refers to the Merrill Lynch EMU Price Return index for bonds. Data for stock market prices and bond prices are quarter-on-quarter growth rates (data available up to the second quarter of 2008). Data on valuation effects are expressed as percentages of total outstanding amounts for investment fund shares (data available up to the first quarter of 2008).

2001 and 2002, shows some important differences. Notably, stock prices also fell strongly in the third quarter of 2001 and the second quarter of 2002, but bond prices, as measured by the Merrill Lynch EMU Price Return index, increased significantly. By contrast, the first quarter of 2008 was characterised by both falling stock prices and only moderate increases in bond prices.

Overall, this analysis highlights the fact that an assessment of the changes in investment funds' asset values benefits from a distinction being made between changes owing to transactions and shifts in portfolio allocations on the one hand, and valuation changes and the underlying asset price movements on the other hand. The calculation of such a breakdown has also revealed that the recent marked decline in the value of investment funds' assets is of a somewhat different nature to those observed in 2001 and 2002.

Three of EMU, such as that recorded in the third quarter of 2001. However, the developments in the second half of 2007 and the first quarter of 2008 are somewhat unprecedented, as for the first time net outflows from investment funds have occurred.

Chart B shows that the valuation effects shown in Chart A are closely correlated with euro area stock price changes as measured by the EURO STOXX index. A one-to-one co-movement is not to be expected, as valuation effects for investment fund shares also reflect changes in stock prices outside the euro area, as well as price changes for other asset categories such as bonds. In particular, the slightly lower amplitude of the valuation effects relative to that of the stock price changes mainly reflects bond price movements, which are less volatile than changes in stock prices. In this respect, a comparison with previous episodes characterised by similar valuation effects, such as those observed in