

Diversified Management Resources in the News

Selected Press Reports on Themes and Practices in Product Distribution and Business Structure

Marsh Non-Deal May Help Putnam Find Footing

Ignites, June 15, 2005

By Marc Hogan

Putnam stands to regain some much-needed stability now that a possible sale or spin-off is apparently off the table, according to industry observers.

With deal rumors quashed, Putnam can focus on bolstering its funds' performance and asset flows as well as holding on to key personnel.

Last Friday, parent company Marsh & McLennan issued a statement indicating that the insurance giant "has no plans" to unload any of its principal business units.

Talk of a possible Putnam sale or spin-off had been circulating for weeks following reports that parent company Marsh was evaluating all of its business units. Putnam CEO Ed Haldeman said that the insurer was indeed considering unloading its fund unit.

That notion was put down, at least for now, with the firm's most recent announcement that no deal is in the works. That should be welcome news for the firm, according to Lou Harvey, president of Dalbar.

"They're probably going to relieve some of the anxiety that's been there depending on who the potential buyer is," Harvey says. "My hope is that it is true and permanent."

However, Harvey says that just because a deal is off the table at the moment doesn't mean that the firm won't go back on the block.

A Putnam spokeswoman referred calls to Marsh. Marsh spokeswoman Barbara Perlmutter declined to comment on the likelihood of a deal taking place in the coming months. However, in the long run she says anything is possible.

Either way, stability is a positive for the firm at this point in time, according to Morningstar director of fund research Russ Kinnel. He says Putnam needs stability to turn around its performance, due to changes in strategy and personnel.

Haldeman, Putnam's CEO, has tried to change the firm's culture since taking over amid the market-timing scandal in late 2003. This year, the firm has seen several fund managers come and go, and investment chief Steven Oristaglio has stepped down.

"It's probably healthy to have this issue resolved," Kinnel says. "It takes years of working together for a team to really click. They need that to happen."

Ultimately, Putnam must improve its performance, according to Kinnel, because it's competing against firms that have better returns and were largely untouched by the scandal. Performance and the ensuing fund sales take time and stability to build, he says.

Putnam had \$28.8 billion in outflows in 2003 and \$26.3 billion in 2004, according to Financial

Research Corp. Money continued walking out the door in the first four months of 2005, accounting for another \$6.8 billion in outflows. The firm's assets under management have declined from \$130.7 billion at the end of 2003 to \$104.4 billion through April 2005.

Flows may not return overnight, but putting the sale rumors to rest should be good for morale, according to **Charlie O'Neill, a recruiter with Diversified Management Resources** and former Putnam managing director.

"It's very positive for a firm of that stature to be determined to maintain its independence," O'Neill says. "As Putnam's performance story strengthens, which Ed Haldeman seems determined to achieve, money will flow back that might have left them."

Jeff Keil, vice president of global fiduciary review at Lipper, says Marsh's decision not to sell Putnam may reveal that the insurance giant sees a recovery in Putnam's ability to generate income.

Marsh's revenues fell last year due to the company's own regulatory troubles as well as problems in its other units. Marsh's operating income dropped 74% in 2004, to \$648 million, according to regulatory filings. That amount includes settlements at Putnam and the costs of Marsh's \$850 million regulatory bid-rigging settlement.

Marsh may still sell or spin off Putnam down the road, Keil speculates. If Putnam can improve fund sales, the fund shop will likely command a higher sales price than it can now. "I would guess they're keeping their options open," Keil says. "I doubt they have made the decision to definitively proceed one way or the other."

AIM CEO Resigns

Ignites, May 18, 2005
By Andrew Greene

Mark Williamson is stepping down as CEO of AIM Management, according to an internal company memo acquired by *Ignites*.

The memo, which was sent yesterday to employees of AIM's parent company, Amvescap, said Williamson will remain with the company until a replacement is found. The memo was signed by Amvescap executive chairman Charles Brady.

"Mark Williamson has shared with me his belief that, in the best interest of his family, and in recognition of the needs of Amvescap, it would be best to begin the process of identifying his successor as CEO of AIM Management and the AIM Division," Brady wrote in the memo.

A spokesman for the firm would not comment further on the reasons behind Williamson's departure. But according to the memo, Williamson will help with the search for his successor while continuing in his current duties.

"To minimize the impact to our business and clients, Mark will continue to guide these groups as we search for a new CEO and provide for an orderly transition over the next 18 months," the memo states.

The search for Williamson's replacement will not begin until Amvescap names a new CEO of its own. The firm has been hunting for a chief executive since Brady gave up his dual role as

chairman and CEO of the firm. A new Amvescap CEO is expected to be named by mid-summer, according to the spokesman.

Williamson joined Amvescap in 1998 and served as CEO of its North American retail business, including Invesco Funds Group, AIM Management and the AIM Division.

During that time, Williamson has been in charge during a difficult period in the company's history. He oversaw Invesco's merger with AIM and was at the helm during the firm's involvement in the fund trading scandal. AIM and Invesco's combined settlement with state and federal regulators totaled \$451.5 million, making it one of the largest settlements of the scandal.

The firm has also struggled with outflows and diminished assets recently. Its U.S.-based AIM and Invesco units have been especially hard hit. AIM finished last year with \$137.6 billion in assets, down from the \$151.1 billion it held at the end of 2003. Meanwhile, Invesco's assets climbed to \$121 billion from \$118.5 billion for the same period. However, \$8.1 billion of that gain was capital appreciation.

The firm's involvement in the scandal also resulted in an executive shakeup. Several top executives left the firm, including Raymond Cunningham, Invesco's former CEO. Cunningham paid a \$500,000 civil penalty for allegedly allowing select investors to engage in market timing. Other executives who left because of their role in fund trading scandal include Timothy Miller, Invesco's former chief investment officer, and Thomas Kolbe, an Invesco senior VP for sales.

Industry recruiters say Williamson's resignation is not all that surprising given AIM and Invesco's troubles over the past couple of years.

"This is an industry in flux at the moment, and change almost breeds change," says Lawrence Lieberman, executive director with recruiting firm the Orion Group. "In general, I'm not surprised. They've had their troubles."

Another factor in the change is the incoming Amvescap CEO. It makes sense that whoever assumes that position will want to appoint the people directly reporting to him, says **Charlie O'Neill, a principal at Diversified Management Resources.**

Williamson cited his family's interests as one of the reasons for his resignation. That's not typically a reason cited for an executive's departure unless there really is a serious issue that individual is dealing with, according to another industry recruiter who wished to remain anonymous.

Either way, there will be a changing of the guard at AIM.

Adoptions, Mergers Thinning Ranks of Funds

Ignites, 08-12-04

By Tom Lesswing

(Excerpts)

Mergers and acquisitions, increased regulatory burdens and belt tightening across the industry continue to cull the overall number of funds available to investors.

While the number of funds are declining, so too are the number of investment firms that offer their own products, due to a steady wave of firms putting their funds up for adoption. Fund mergers and liquidations are gobbling up a large number of funds. So far this year, 234 funds, not including share classes, have been either liquidated or merged out of existence, according to data from Lipper. That's on the heels of the 597 funds that were liquidated or merged away in all of 2003.

The Investment Company Institute's numbers show a similar phenomenon. At the beginning of last year, there were a total of 8,244 funds. By the end of last year that number had been whittled down to 8,126.

While the trend of mergers and liquidations shows no signs of abating, fund adoptions are continuing to move full steam ahead.

"I think it's safe to say that interest in fund adoptions is at an all-time high," says Neil Bathon, president of Financial Research Corp.

Most funds that are put up for adoption are smaller, with decent performance track records but weak distribution outlets. A larger company with access to distribution will adopt the fund, taking over the fund administration, distribution and recordkeeping responsibilities. That lifts a huge cost burden off of the fund's erstwhile advisor who is generally retained as a sub-advisor to continue managing the fund.

Helping drive the fund adoption trend is an onslaught of new rules and regulations being issued by the SEC. In July alone, a handful of firms began the process of handing their funds over to other companies.

Hillard Lyons agreed to have Constellation Investment Management take over its \$36 million Large Cap Quality Growth Fund. The fund received four-stars from fund tracker Morningstar. As part of the arrangement, Hillard Lyons, which is the fund's current advisor, will serve as sub advisor to the fund and Constellation Investment Management, the advisor to the Constellation Funds, will become the advisor.

The arrangement will allow Hillard Lyons to focus on asset management rather than on fund distribution, shareholder service and administration, says James Allen, chairman and CEO of Hillard Lyons. While being able to focus on asset management, Hillard Lyons will also benefit from distribution through Constellation.

Hillard Lyons began evaluating putting its funds up for adoption two years ago, primarily to get better distribution and to have another firm handle the non-investment functions of running funds. Costs of complying with a wide range of regulations stemming from the market timing scandal only increased Hillard Lyons' interest in being adopted, Allen says.

Many other fund sponsors are in a similar boat, says **Charlie O'Neill, with Diversified Management Resources**. One recent rule, for example, requires fund firms to appoint chief compliance officers. It's not unusual for such executives to command a \$300,000 salary. Fund firms are also facing increased distribution costs.

As more fund firms agree to adoptions, some industry observers question if jobs will be eliminated.

Bathon, however, maintains that most fund firms that are putting their funds up for adoption are staffed to a bare minimum. That means they have few, if any, employees to cut after handing over their funds.

"I think the two groups of people who are impacted are the compliance and distribution people," adds John Grady, CEO and president of the Constellation Funds. "Most of the time, you have adoptions because firms don't want to invest in compliance and distribution."

Adoptions, Mergers Thinning Ranks of Funds

Ignites, Aug 3, 2004
By Tom Leswing

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"This gives us an opportunity to open up that process on a much broader scale," Allen says. "And

in this case, we think shareholders will see an improvement."

As part of the change, fund shareholders will be able to exchange fund shares for other Constellation funds and vice versa, he says.

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Many other fund sponsors are in a similar boat, says **Charlie O'Neill**, an executive recruiter with **Diversified Management Resources**. One recent rule, for example, requires fund firms to appoint chief compliance officers. It's not unusual for such executives to command a \$300,000 salary. Fund firms are also facing increased distribution costs.

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As more fund firms agree to adoptions, some industry observers question if jobs will be eliminated.

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Hillard Lyons, of course, isn't alone in putting its funds up for adoption.

The World Funds of Richmond, Va., are preparing to merge the Chase Mid-Cap Growth Fund¹ into the Adviser Series Funds of Milwaukee. The fund, which is not affiliated with JP Morgan Chase, held only \$6.7 million in assets as of March, according to the fund's semi-annual report. For the year ended June 30, it had posted a solid 22.89% return.

An SEC filing says that the fund's advisor, Chase Investment Counsel Corp., believes that handing the fund over to Adviser Series will help it achieve economy of scale savings. That may help the fund lower its fees over time. Chase Investment Counsel Corp., which is the current advisor to the fund, will continue to manage the portfolio.

Other recent fund adoptions include Pitcairn Financial Group's decision to hand its funds over to Constellation. In March, Cooke & Bieler also joined in the fund adoption party. It handed its C&B fund family, which had approximately \$529 million, over to Wells Fargo.

Mergers are serving to shrink the ranks of funds. Affiliated Managers Group's Managers Funds recently announced that it was acquiring the Fremont Funds, holding approximately \$3 billion in assets. The Seix Classic Funds are also disappearing as a result of a merger. The funds have been acquired by Trusco Capital Management, which is part of SunTrust Bank. As part of the deal, the Seix Funds will be merged into Trusco's STI Classic Fund family.

The \$390 million Golden Oak Funds also decided to throw in the towel on running funds. Rather than put its funds up for adoption, however, it decided to have the funds merged into funds from Goldman Sachs and Federated.

Federated isn't stopping there. It's planning to acquire three additional funds from Banknorth Funds. According to SEC filings, Federated is planning to merge the Banknorth Large Cap Core

Fund² into the Federated Capital Appreciation Fund³. It also wants to merge the Banknorth Small/Mid Cap Core Fund⁴ into the Federated Kaufman Fund⁵. Federated is also proposing to merge the Banknorth Intermediate Bond Fund⁶ into its Federated Total Return Bond Fund⁶.

National City, meanwhile, has acquired Provident Financial Group and is gearing up to absorb fund assets from Provident's Riverfront Fund family. Under that arrangement, assets from six Riverfront funds will be merged into existing funds offered by National City's Armada Funds.

Other moves to trim fund lineups represent firms cleaning up their existing line of products.

Last month, for example, ING proposed merging its High Yield Opportunity Fund⁷ into the High Yield Bond Fund⁸.

Scudder is also shedding the number of funds it offers. In July, it started the process of merging its Scudder 21st Century Growth Fund⁹ into the Scudder Small Company Value Fund¹⁰. According to an SEC filing, board members for the Scudder funds believe that both funds have similar investment mandates. The funds also use the same portfolio manager.

Also last month, Scudder proposed merging its Scudder Municipal Fund¹¹ into the Intermediate Tax/AMT Free Fund¹² and the Scudder Technology Innovation Fund¹³ into the Scudder Technology Fund¹⁴.

It also wants to merge the Scudder Large Company Fund¹⁵ into the Scudder Large Cap Value Fund¹⁶.

Morningstar has never been afraid to bite the hand that feeds it

Newsday (7/11/04)
By Tami Luhby

(Excerpts)

When trading scandals embroiled the mutual fund industry over the past year, the Chicago-based research firm blasted the companies involved.

Invesco Funds "don't deserve investors' money," it told investors.

Putnam Investments' actions, Morningstar said, were "absolutely appalling."

And it lambasted Federated Investors for its "shocking lack of oversight," which Morningstar said "defies belief."

The fact that Morningstar levels such withering criticism may not surprise individual investors, who have long looked to the 20-year-old firm for its frank opinions of funds. What's less obvious is that those three mutual fund companies are also Morningstar clients who pay the firm hefty fees for services such as advice for their retirement plan clients and for data and research.

But Morningstar is much more than just a fund-rating firm these days. It now serves hundreds of financial institutions, which represent a growing portion of its income. What's more, Morningstar recently announced plans to go public to fuel further expansion -- and likely put its shares in the

hands of the same companies that it rates.

These dealings raise the possibility of conflicts of interest since sales of services and data to fund families and other financial firms now account for the largest chunk of Morningstar's revenues. This could mean Morningstar will start lobbing softballs at the fund companies instead of grenades.

"It creates a perception and credibility problem," said Burt Greenwald, a Philadelphia-based mutual fund consultant, though he believes Morningstar remains objective. "It's a very difficult tightrope to walk." ...

A good reputation

At this point, Morningstar's reputation for objective advice remains intact, industry experts say. But the company must be vigilant in protecting that image as it grows and as it faces new pressures of being publicly traded.

This is especially critical if Morningstar wants to capture a share of the \$432.5 million that Wall Street brokerage houses set aside for independent research as part of the global analyst research settlement, as it is hungry to do. As part of a deal finalized last year, the big brokerage firms agreed to distribute independent research, alongside their own, to retail clients. The settlement came after New York Attorney General Eliot Spitzer uncovered evidence the brokerage houses were issuing biased research reports in hopes of boosting their investment banking business.

Morningstar has already scored its first deals under the settlement. Merrill Lynch and Goldman Sachs will distribute the firm's independent stock research to their clients. To get more of these, Morningstar must stay above question.

"The value of their brand is their biggest asset," **Charlie O'Neill**, principal at Diversified Management Resources, a Boston-based financial marketing firm, said of Morningstar. "There's never been any evidence that their rankings, ratings or information services have been anything less than objective." ...

Pressure on Fund Marketing

Money Management Executive (1/19/04)

With the industry heading toward almost assured legislation relating to fees, the way funds market themselves is sure to morph, and some in the industry are bracing for a "revolution."

Regulators have put the way fund companies conduct business under the microscope since the fund scandal hit the headline news pages in September and, even before Fund, legislation proposing increased fee transparency was proposed in the House. Directed-brokerage agreements, soft-dollar arrangements, 12b-1s and other fees are among the practices under scrutiny.

However, the potential elimination, or limitation, of 12b-1 fees - which are one way a fund firm can pass along marketing costs to an investor - would pose significant problems for some fund firms.

The Perfect Storm

Ted Siedle, president of Benchmark Advisory Services in Ocean Ridge, Fla., said the economics of distribution are changing dramatically and the combination of a heightened regulatory environment and rampant abuses in the industry are the makings of the mutual fund industry's version of "The Perfect Storm."

"Most funds don't have spectacular performance, so it's a marketing game. It's always been a marketing game. That's got to change," said Siedle, a former Securities and Exchange Commission attorney and onetime Putnam Investments chief of compliance.

Siedle expects downward pressure on both fees and trading costs. "I think the use of fund brokerage commissions for distribution or marketing will be virtually prohibited," Siedle said. (See the ICI's call for the eventual total abolition of directed-brokerage, page 12.)

"How will funds pay for marketing and research they have been soft-dollaring? The fund companies are going to try and impose fees and loads where possible to make up the difference. If they can impose redemption fees and transfer fees or sales loads to pay for marketing, that will give brokers an incentive to distribute certain funds," Siedle said.

"I think the industry has got the biggest marketing challenge since the mutual fund boom began," he added.

Lou Harvey, president of Dalbar, Boston, is also bracing for a big quake in the industry. Harvey expects a revolution, rather than an evolution, in relation to regulation and marketing.

Harvey said there are two regulatory approaches to correcting the industry's problems in this area. One way is to look at each individual fee, soft dollars, trading costs and front-end loads. "There are a lot of different pockets there," Harvey said.

The other way is to take a macro approach. There is a provision in the 1940 act that prohibits competitive pricing. By eliminating that restriction, a lot of the problems can be resolved, Harvey said. "It will be interesting to see if people think we can just tweak the system," he said.

"It would be my hope that competitive pricing is restored and, therefore, the broker/dealer firms will get compensated directly, rather than from the fund companies," Harvey said. He does not expect fund companies to make investors pay for marketing in the future via some other fee paid to the fund complex. "In the future, the distributor will collect their own fee, similar to the structure in managed accounts. It seems logical," he said, adding it will be up to the investor to shop around for best prices.

Jeff Fishman, founder of JSF Financial, a financial planning firm in Los Angeles, said that he expects investors will end up paying virtually the same cost, whether it is through a 12b-1 fee or a heightened management fee. He doesn't see the dynamics of distribution changing all that much, either. "In the end, regulators can require all the disclosure they want, but the most important thing for investors is the investment adviser they work with. Are they working with good, ethical, people?"

A reduction in fees by fund firms will place pressure on some budgets, said Dan Sondhelm, vice president and partner with SunStar, a strategic communications firm in Alexandria, Va. However, Sondhelm doesn't see doom and gloom. "In the short term, clearly revenues will decrease if everyone lowers their fees by 20%." However, over the long run, Sondhelm thinks companies will be more competitive after regulators are done clarifying what arrangements are acceptable.

Several mutual fund firms, including Fidelity Investments, Dreyfus Corp. and Janus Capital, declined to be interviewed for this article.

Pinching Pennies

Meanwhile, pressures placed on fees that are used to market funds may put a squeeze on sales marketing personnel, including wholesalers, cautioned **Charlie O'Neill**. Firms will be examining every one of their marketing efforts and looking at ways to trim costs. Firms will evaluate the number of necessary field wholesalers and potentially move some of that work to an inside sales team or have it handled electronically.

O'Neill also expects fund firms to scrutinize the way they distribute literature, he said, noting the high cost of shipping. Additionally, there will be more opportunities for outsourcing on the marketing side, O'Neill said (see related article on operations outsourcing, page 6). "Does a mutual fund company need 50 marketing writers on staff, taking a fixed cost, when outsourcing that work would make it a variable cost?"

However, O'Neill warned against regulators getting overzealous and trying to regulate fee amounts or percentages, such as the "inappropriate" settlement Alliance Capital entered into with New York Attorney General Eliot Spitzer. "When regulators tell private companies how much they can charge for their services, that's called communism," he said.

However, some don't expect the giant U.S. mutual fund machine to just let profits walk away. "The mutual fund industry is the most profitable industry I know, and there is a reason for that," said Brent Glading, founder of Montclair, N.J.-based pension consultant Glading Group. "Their profit margins will be aggressively protected. I don't see an industry that has been operating this way for decades changing because Eliot Spitzer scratches the surface."

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Confirming sound investment choices (**Newsday** 7/27/03) Interviewed for an article providing advice to investors, O'Neill described the importance of finding a qualified financial advisor.

Defining Business (**Money Management Executive** 10/14/02) "Many fund companies are at a crossroads, according to Charles O'Neill, president, Diversified Management Resources. In order to keep costs down, many complexes that built out during the boom years of the 1990s are going to have to drop part of their business and concentrate more on specific areas, O'Neill said. 'Fund companies are going to have to decide essentially whether they are product distributors or product manufacturers.'

Is Fund Marketing an Oxymoron? (**Mutual Fund Market News** 2/04/02) As equity indexes struggle to hold onto gains and recovery seems to be well hidden around the next corner, marketers have found themselves in an unfamiliar world. A report from Diversified Management Resources, suggests that new tactics are required to reach investors who were burned in the recent bear market. A few companies that have marketed themselves successfully may point the way for the rest of the industry.

New Study to Review Marketing Service Providers (1/18/02) Diversified Management Resources has announced that it is undertaking a comprehensive study of companies providing document management, printing and fulfillment, and related marketing services to mutual fund companies. As described by D.M.R. principal Raymond O'Brien, the study is being conducted because, as the traditional lines of distinction between printing and fulfillment companies have blurred, mutual fund marketers are no longer aware of the full scope of services available to them. He also noted that many new companies have emerged as high quality, cost-efficient vendors in this market. The study will be sponsored by service providers and offered free of charge to the top 100 mutual fund companies.

Tighter Marketing Budgets (1/14/02) Discussing mutual fund companies' 2002 marketing budgets in [Mutual Fund Market News](#), ("Funds Streamline Marketing Budgets") (1/14/02), Charlie O'Neill observed that most fund companies establish two or three alternative marketing budgets, each responding to a different revenue scenario. He said companies will maintain a base line of promotional and informational materials for use by financial advisors, then add 'nice to have' marketing projects as the year's revenue forecast is adjusted.

Flawed Fund Distribution? (10/29/01) In an article on marketing strategies for the current difficult business environment in [Mutual Fund Market News](#), (10/29/01) O'Neill said the past practice of most mutual fund companies focused on sales efforts built around short term product performance is unlikely to work in the future. He also noted that mutual fund companies must develop a clear sense of their value proposition – the compelling reasons why customers should consider doing business with them – as they devise their new marketing strategies.
