3 Ways to Buy the Index

Description

A sad truth about investing is that most professionally managed funds underperform their respective benchmark. And that will certainly remain the case. For this reason, buying an index is a great option for many investors. This is especially the case for those who don't want to pick individual stocks.

But even stock pickers can benefit from adding an index to their portfolio. Indices can be a great way to diversify, and it can also provide exposure to other markets where selecting individual names is more difficult (such as emerging markets). Sector-specific ETFs can provide exposure to industries where analyzing individual names can be overly complicated, such as financial services.

But what is the best way to buy them? It depends what kind of investor you are. Below are three appealing options.

ETFs

For anyone who also picks individual stocks, this should be the automatic go-to option. Because ETFs have a regular ticker on a major exchange, they can be bought just as easily as stocks and held in the same portfolio.

The leader in the ETF space is iShares, which provides plenty of options. For example, investors looking to buy the TSX can add the **iShares S&P/TSX Capped Composite Index ETF** (TSX: XIC). Looking for exposure to energy companies only? Then you can buy the **iShares S&P/TSX Capped Energy Index ETF** (TSX: XEG).

The good news about ETFs is the low fee. For example, the Capped Composite ETF has an annual fee of only 0.05%. The bad news is that there is little incentive for financial advisors to use them.

Bank index funds

There are some people that like having their savings at the same place as their bank account. It can be a lot easier to manage. And for those investors, the banks offer index funds as well.

The bank index funds are a little more expensive than ETFs like iShares, but are still reasonably priced. The lowest-priced bank index funds come from **TD** (TSX: TD)(NYSE: TD) through the "e-series" funds. For example TD's Canadian Equity index fund comes in with a 0.33% MER. But again, just like the ETFs, you shouldn't count on any financial advisor pushing it.

Fee-only advisors

Financial advisors will counter that their clients, despite paying higher fees, are getting a good deal. This is because advisors provide not only investments but also valuable advice, such as savings goals, tax planning, estate planning, and more.

But there is growing popularity in hiring fee-only advisors and paying them an hourly rate, typically $100-$250 per hour. This can be a bargain. For example, if someone is investing $100,000 and only needs a couple hours of advice per year, that amounts to 0.5% of his portfolio or less. This is much lower than the fee he would pay on any mutual fund.

And without any conflicts of interest, these advisors will be more than happy to help you select the right ETFs.

Foolish bottom line

Each of these options has its own pluses and minuses; the best approach depends on what kind of investor you are. But the three strategies have one thing in common: they're a better choice than investing in most mutual funds.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:TD (The Toronto-Dominion Bank)
2. TSX:TD (The Toronto-Dominion Bank)
3. TSX:XEG (iShares S&P/TSX Capped Energy Index ETF)
4. TSX:XIC (iShares Core S&P/TSX Capped Composite Index ETF)

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Author
bensinclair