3 Reasons to Never Invest a Penny into Mutual Funds

Description

As of February 2017, Canadians have $1.3 trillion invested in mutual funds. Year after year, Canadians put their trust in fund managers in the hopes that an experienced professional can outperform the market. Should investors who feel they don't have the time to manage their investments invest in mutual funds?

The answer is no, and below are three reasons why investors should never invest in mutual funds.

Underwhelming performance

Historically, the strong majority of mutual funds haven't outperformed the stock market. There is a better chance of getting an ace when you have 20 at the blackjack table than you do selecting a mutual fund that consistently outperforms the market! Even if a fund outperforms one year, it typically fails to do so the following years.

Why can't a fund manager, who monitors and has superior knowledge of the stock market, provide superior returns for investors? It's because the future outcome of markets is unpredictable. No matter how experienced a fund manager may be, he or she can never consistently anticipate the market's behaviour.

Unless Peter Lynch is managing the mutual fund, it's highly unlikely it can consistently deliver above-average returns to investors.

High fees

As Foolish investors know, the power of compounding interest is a beautiful phenomenon. However, the power of compounding investment fees can be detrimental to an investor's portfolio. Most mutual funds charge a fee of around 2% of the entire fund. This may seem like a small portion, but its impact over time can be significant.

Capital gains tax

The majority of mutual funds are actively managed. Therefore, managers of the funds are continually buying and selling stocks to try and outperform the overall market's returns. However, every time a stock is sold above what it was bought for, a taxable capital gain is triggered. Therefore, investors are left having to pay taxes on 50% of each gain the fund generates, unless it's held in a TFSA, RRSP, etc…

Between the fees incurred and taxes paid, any returns the fund generates are being eroded by the fund manager's transactions.

Foolish bottom line

Buying and holding fantastic companies such as **Fortis Inc.** (TSX:FTS)(NYSE:FTS) and **Toronto-Dominion Bank** (TSX:TD)(NYSE:TD) has provided better returns for investors year after year. There are obviously some mutual funds that can outperform the market from time to time; however, it's important to maintain a long-term view and stick with securities that consistently provide solid returns.

Fool on!

CATEGORY

1. Investing

POST TAG

1. Editor's Choice

TICKERS GLOBAL

1. NYSE:FTS (Fortis Inc.)
2. NYSE:TD (The Toronto-Dominion Bank)
3. TSX:FTS (Fortis Inc.)
4. TSX:TD (The Toronto-Dominion Bank)

PARTNER-FEEDS

1. Msn
2. Newscred
3. Yahoo CA

Category

1. Investing

Tags

1. Editor's Choice

Date
2025/08/26
Date Created

2017/03/29
Author
cbeck