Should You Give Up On Shares And Just Buy Funds?

Description

Deciding whether to invest in funds or shares can prove to be a difficult decision for many investors. While funds offer a simple means of diversification and potentially require less time to analyse and manage on an ongoing basis, they can be costly and deliver sub-optimal investment performance. As such, shares are often viewed as more appealing by many investors.

However, with stock markets across the world now trading at or close to record highs in many cases, is it time to 'trust the professionals' and buy units in funds, rather than shares in companies?

An uncertain outlook

The outlook for the world economy is highly uncertain at the present time. After a Bull Run in many stock markets across the globe, there are fears that valuations may now be excessive in certain regions and sectors. Therefore, some investors may feel that now is the right time to back the experts through buying funds, since they may have a better chance of identifying favourable risk/reward opportunities in what may be a seller's market.

While there may be an essence of truth in the idea that valuations are relatively high, the reality is that the outlook is always uncertain for the global economy. Even at times where it feels relatively stable, world economic growth can be hit by a one-off event, or by a financial crisis which turns into a global recession. Therefore, the idea that the current outlook is more favoured to buying funds rather than shares may be fundamentally flawed.

Cost disadvantages

Of course, many fund managers are successful at their jobs and have strong track records of outperforming their benchmarks. The problem, though, is that in many cases the costs to access this outperformance are prohibitively high. In fact, in some cases an annual charge of 1%+ can wipe out any outperformance of a benchmark which is offered by a fund. In this scenario, it may be more profitable to simply buy shares rather than invest in a fund.

This argument is enhanced by the low dealing charges which are now available on shares. With the advent of the internet, sharedealing charges have slumped. While funds are now cheaper to buy than they once were, management charges can still be excessive.

Practicality

Perhaps the main advantage of funds versus shares is their simplicity and practicality. An investor can gain exposure to tens of companies in just one fund, which reduces company-specific risk and may lead to a more favourable outcome. To mimic this level of diversification, an investor would need a large amount of capital, which is often not available.

Furthermore, funds require less time commitment from an investor. The fund manager will conduct the research and due diligence into the stocks in the fund, which means the investor can spend their time in other pursuits. In contrast, shares require monitoring and evaluating, which sometimes dissuades people from buying them.

However, even funds need to monitored, and investors must research which funds to buy. Therefore, the differential in terms of time spent managing shares versus funds may not be all that different. Alongside their lower costs and the fact that there is never a perfect time to invest due to ever-present uncertainty, shares could prove to be the more attractive of the two options for many investors in the long run.

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