

## Easy steps to understanding mutual funds

Most of the people I meet know what a term deposit or a guaranteed investment (GIC) is.

The single most asked question concerning investment vehicles is "What is a mutual fund or investment fund?"

To answer this, let me tell you the story about:

### "THE PRUDENT FARMER"

Once a very prudent and successful farmer decided that he should become an investor. After diligent study and research, he concluded that he lacked the necessary time, knowledge and experience to be a successful investor. Thus he determined to seek the advice of an expert.

Finally, he presented himself at the offices of Bull and Bear Limited, professional investment counsel, and asked to see Mr. Bull, the president. He was somewhat taken back upon entering a board room to find five distinguished gentlemen seated around a long table. After being cordially received and introduced, the farmer began:

"Gentlemen, I am here because I have a proposition to make. Over the years I have been able to set aside a nice little sum of money which I have decided should be invested. Various inquiries and a certain amount of reading have brought me to the conclusion that you gentlemen are recognized as the best there is in the field of investment management. Therefore, it is to you that I have decided to make my proposition. I wish to give you all of my money to invest. However, there are certain conditions I ask in so doing.

"First," he said, "I don't wish to have all my eggs in one basket. Experience has taught me that the only way to farm successfully is to diversify your crops and your livestock.

Therefore, I want you to study all of the industries in our economy, selecting those which in your opinion offer the most potential to the investor. Then I want you to look closely at all of the companies within each of these industries, picking out the most promising. Having done this, I want you to compare the various companies of the various industries, so that you can determine 60 to 70 of the best corporations in which to invest.

"Once you have done this, however, I don't want you to stop. Things can change quickly. So I ask you to make this a continuous full-time comparative study. I will give you authority to make any changes you wish, whenever you think such changes will benefit me.

"Incidentally," he added, "I've always found that you can acquire a great deal more information by talking to a man face to face. Therefore, I want you to go out to these companies you study and talk to the people who run them...the accountants, the production people, the sales staff and so on.

"Second," he stated, "you should look after such things as dividends, rights, warrants, and taxes. You keep the securities and handle all of the paper work. All I want is periodic dividend cheques and a statement each year telling me how to report for income tax purposes.

"Third, I expect you to agree to an audit of my affairs - by my auditors - every year. I also wish to receive statements, along with my dividend cheques, telling me all about what has happened during the previous months, such things as what you have bought, what you've sold, what your expenses have been and how

much I've made or lost. I would also appreciate your opinion on the outlook for the next three months.

"Finally," he stated, "I know that this is going to cost me money and you have every right to be paid. As an incentive to you, and a protection to me, I suggest that you retain as your fee, 1/2 per cent per year of whatever my investments are worth. In this way, the more you make for me, the more you'll earn for yourselves. At the same time, I will be protected in that, percentage-wise your fee will remain constant.

"This then, gentlemen," he concluded, "is my proposition."

After thanking the farmer for the compliment of selecting Bull and Bear for this proposal, Mr. Bull then briefly summarized the proposition:

1. Continuous full-time investment management;
2. Complete responsibility for the administration of all detail work involved;
3. The preparation of quarterly reports and the submission to a complete annual audit by the farmer's auditors;
4. The calculation and mailing of periodic dividend statements and the preparation annually of an appropriate statement for income tax purposes;
5. The retention, as fee, of an amount equal to 1/2 per cent of the market value of the portfolio annually.

Agreeing that all was understood, Mr. Bull asked:

"Now Sir, would you be kind enough to indicate the amount of the responsibility you wish to entrust with us."

"\$1,000," the farmer replied. An awkward silence followed. In a moment, with an embarrassed

clearing of his throat, Mr. Bull said:

"One of our greatest sources of pride has always been our sincere interest in the affairs of our clients...interest which has compelled us to provide the wide range of services you have requested. However, we are in business, and being in business, our very existence depends upon the making of a profit. Being a reasonable man, I am sure you understand this.

"As you look around, you will see that there are five of us. Now 1/2 per cent of \$1,000 amounts to \$5, which means that the most we could receive, at the outset at least, for the time and effort that would be required if we were to accept your proposal, would be \$1 each.

"In all fairness and honesty, I doubt that we could readily accept.

"On the other hand," he added, "perhaps you could interest a number of your friends and acquaintances in your idea. By combining a large number of \$1,000 amounts, you could put us in the position of being able to do as you ask."

Seeing the merit in Mr. Bull's suggestion, the farmer thanked them and left. For the next few weeks, he devoted most of his time to explaining his idea to friends and acquaintances. Although many were interested and willing to pool their money with his, he soon realized that by his effort alone it was going to take a long time to build this pool of investment capital to a sufficient size. It was at this point he had another idea.

By so doing, he could spread his story in wider and wider circles and thereby greatly enhance the possibility of gathering together a sufficient amount of money.

Once again, being a reasonable man, he realized this would cost money. He considered many possible methods of obtaining the necessary money to cover these costs. Bearing in mind that:

1. The people who were to benefit from this undertaking would have to be the ones who paid;
2. If the charges were too high, people would refuse to pay and his idea would fail;
3. If the charges were too low, he would be unable to meet his costs and thereby suffer a heavy personal loss.

After considerable deliberation, he decided upon a very simple, sensible method of charging. He decided to form an organization or club. Membership would comprise those who contributed their money to the "capital pool". To hear and learn about the organization, its purposes and possibilities would cost nothing. To join the club, however, one would have to pay a one-time membership fee of an amount equal to 9 per cent of the capital contributed. Out of his one-time membership fee would come all the costs of marketing and distribution.

The result? You've probably guessed. A mutual fund was born, based on the age-old principles so well understood by the prudent farmer.

Thanks to The Investment Funds Institute of Canada, Education Division, for the story of "The Prudent Farmer".

# WHY FILE A TAX RETURN?

**NEW! Tax Credit!**

The new Federal Sales Tax Credit is available to people with little or no income but only when a federal tax return is filed.

Many persons over 18 years and seniors who do not file income tax returns because of little or no income should strongly consider doing so this year because they too may be eligible for this credit.

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# ANNOUNCEMENT



Mr. Bruce Field, C.L.U., Branch Manager, is pleased to announce the appointment of Tom Shillington as a new associate to the Brampton Office.

Tom will be representing the Mutual Life of Canada and affiliated companies, offering a broad range of financial plans and services, including life and disability insurance, R.R.S.P.'s, other savings and investment plans, group benefits and financial counselling.

**Mutual Life of Canada**

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