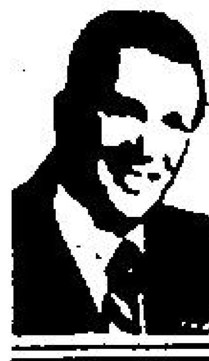
Patience a virtue in mutual fund investing



IT'S YOUR MONEY

Paul J. Rockel

Note: This is an article written three years ago, but in light of current economic conditions bears repeating.

What is the most important item to realize if you choose to invest in mutual funds?

Did you answer "rate of return?"

If so, you were wrong. We realize that the rate of return over the long term of good equity mutual funds have proven them to be a sound investment. Some have averaged 15% or better over time. But, that doesn't mean they will average 15% ever year. Some years there will be gains of 25% or even 35%, other years there will be very little gain, and some as in 1990 a loss. It is our belief that in every 10 year period there will be a minimum of two, or as many as four, poor or negative years.

Nevertheless, we believe that mutual funds have a public record of giving the best return of any type of commonly available investment where your assets are looked after for you. We admit that if you were smart (or lucky) enough to invest in the right stock, or that special piece of real estate, or the game of Trivial Pursuit, you would do better. But, how many of us know about those special situations, and even if we do, after we take our profit is the next investment going to win or lose for us?

Here is a true story about a mutual fund investor who invested $71,000 in June 1973. We'll call him "Mr. Patience." Now for comparison we'll use an imaginary "Mr. Scared" who made the same investment at the same time.

Both 1973 and 1974 were down years in equity markets, another recession! Both Mr. Scared's and Mr. Patience's value fell. Their values fell from $71,000 to around $50,238 by December 31, 1974. Needless to say, both were completely dissatisfied with the investments (can you blame them?).

Mr. Scared decided that he was going to cash out, despite being advised against it by his financial advisor. *He cashed out.*

Mr. Patience also wanted to cash out, but he listened to the advice to stay in the fund, and he did. (Later, when the fund value returned to $71,000 he originally invested, he wanted to cash out again, but again he listened to the advice of his financial planner who advised against it and left his money in the fund.

A little over four years ago (1984, or 52 months) Mr. Patience retired and said that he wanted $2,000 per month sent to him from his mutual fund. It's called a monthly withdrawal plan and as this money was not in an RRSP it was taxed very lightly (because Mr. Patience still had his $100,000 capital gains deduction). If the money was in an RRSP, it would have been taxed as income.

By the end of 1987, he had received $104,000 in monthly cheques ($2,000 monthly times 52 months) and the remaining value in his mutual fund account was $583,563.

Mr. Scared on the other hand, cashed out his $50,238 at the end of 1974 (he had invested $71,000). Let's suppose in the 13 years to the end of 1987, he had averaged 12% interest at the bank. It would now be worth $219,214. Of that $148,214 would have been taxable interest, and if he was in the 30% tax level, it would have cost him $44,464 in taxes ($74,107 if he was in the 50% tax bracket).

In answer to the question at the top of this article, I think we can say that time (or patience) is the most important element in mutual fund or most other forms of investing. We should look at a mutual fund as an investment for a minimum of five years (preferably a lifetime as Mr. Patience has), despite the fact that you can retrieve your value at any time.

The above story about Mr. Patience is true. How many would do what the imaginary Mr. Scared did? I think you'll agree, patience was well rewarded.

Yes, I think we can say that patience has its virtues (in mutual fund investing).

For a free booklet on mutual funds in an RRSP and a chart comparing the performance of an actual mutual fund with a 10% investment over the last 23 years, contact Peter C. Masson, M.B.A., Regal Capital Planners Ltd., 10 Fagan Drive, Georgetown, Ontario, or phone 877-7216.

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