Champions for Financial Legacy

BUYING COLLECTIONS IN THE MARKET

INTRODUCTION

Our recommended entry strategy into the stock market is to “buy collections.”

Instead of purchasing shares of individual companies, investors can buy shares of collections, like mutual funds or ETFs, that include many companies. We suggest this approach because it offers **lower risk**, **lower cost**, and the potential for **higher returns**.

The worksheets in this section will help you understand how investing in collections works.

SECTION 1: TYPES OF COLLECTIONS

You can buy collections of stocks in two main ways: **mutual funds** and **exchange-traded funds (ETFs)**.

Mutual funds pool money from multiple investors to buy shares of various companies. ETFs also represent a collection of companies, but they trade on the stock market like individual stocks.

While both are used to invest in collections, ETFs are now more commonly used than mutual funds.

SECTION 2: ATTRIBUTES OF COLLECTIONS

Both mutual funds and ETFs are constructed to offer investors many benefits, including:

- **Diversification:** This is one of our four rules of investing that we always follow.
- **Low Fees:** This is another one of our four rules. Funds have low fees, with some funds costing only pennies.
- **Automatic re-investment:** Just about all funds will re-investment your dividends and buy more shares with no administrative costs. This fulfills another of our rules.
- **Professional Managers:** Most of us lead busy lives, and we do not have the time to devote to our investments. Funds are led by professional managers who monitor their portfolio almost 24-7 every day.

SECTION 2: ATTRIBUTES OF COLLECTIONS

- **Liquidity:** Funds are very liquid. Monies received from redeeming mutual fund shares are in your account the next day. Funds from ETF sales have a 3-day clearing process.

- **Low minimum investments:** There are many funds that have a minimum investment of $1. You do not need a lot of money to start invesiting.

- **Safety:** Fund accounts are audited on a quarterly basis. You are protected against losses by theft or fraud (SPIC).

In Section 2, we explore key attributes of collections.

Review the list and choose the two attributes you value most. Write them below and briefly explain why they're important to you.

SECTION 3: PASSIVE AND ACTIVE MANAGEMENT FUNDS

All funds are categorized as either actively- or passively-managed.

- **Actively Managed Funds** have a fund manager(s) choosing what stocks to buy for the fund. In theory, you are paying for the stock choosing expertise of the manager.

- **Passively Managed (Index) Funds:** There is no fund manager choosing stocks to include in an index (passively-managed) fund. The fund will simply replicate the index it represents. Example: All S&P 500 Index funds have the same 500 stocks (that make up the index) in them.

Cost & Performance Comparison

Let's compare the two types of funds on cost and performance. On average, actively managed funds have a cost 10 times that of an index fund. The cost difference is because in an actively managed fund you are paying for the expertise of the fund manager. That is fine, but then you should expect an actively managed fund to outperform an index fund. Unfortunately, this is not true. Only 5% of actively managed funds outperform their index over a 15 year period. So not only are index funds less costly, they actually outperform almost all actively managed funds.

Challenge: Use the worksheet below to compare the cost and performance of passively managed (index) funds and actively managed funds.

We’ve filled out the first row as an example to show you how it works.
To complete the rest, look up the fund's trading symbol (like “VOO”) and search for its fees and 5-year return. *Example search: “VOO ETF fees and performance”*

SYMBOL	TYPE	NET EXPENSE RATIO	5 YEAR RETURN
VOO	INDEX	0.03%	18.56%
MOAT	ACTIVE	0.47%	12.75%
VBR	INDEX		
DFSV	ACTIVE		
VUG	INDEX		
SPGP	ACTIVE		

SECTION 4: KEY TAKEAWAYS

1. Purchase Stocks in Collections: When entering the stock market, it's better to buy collections of stocks (like mutual funds or ETFs) rather than individual stocks.

2. Advantages of Purchasing in Collections: These include lower risk, professional management, lower cost, liquidity, and added safety.

SECTION 5: ACTION PLAN

🔎 DO YOUR RESEARCH

Investing requires research to help you reach your financial goals.

Answer Key:
Section 3: VBR INDEX 0.07% 14.95%; DFSV ACTIVE 0.30% 10.82%; VUG INDEX 0.04% 16.51%; SPGP ACTIVE 0.36% 14.90%