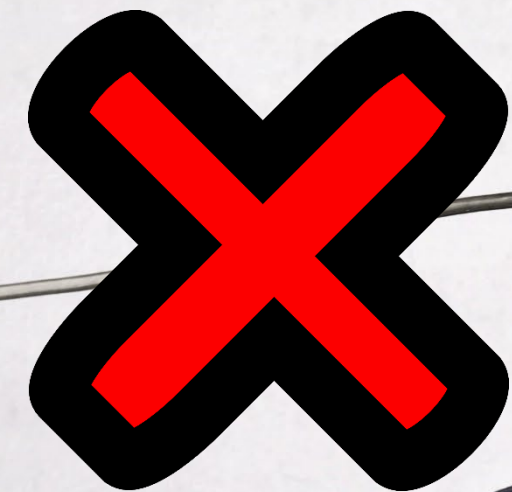


**Rely on others too  
much**



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# Learning outcomes

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- Know the three questions every investor should answer
- Learn what a mutual fund is
- Understand the difference between an active and passive fund

# Learning outcomes

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- See the performance to expect from different funds
- Understand your chances of picking a winning actively managed fund



# Questions to consider before buying stocks

- ★ If you think you want to pick your own stocks, answer these questions:

# 1. Are you interested in picking stocks?

- ★ My nieces are not
- ★ If you have no interest, why waste your time?

## 2. Do you have time to pick stocks?

- ★ Picking stocks is not easy!
- ★ You cannot make money by just reading the newspaper and selecting a stock that looks good

## 2. Do you have time to pick stocks?

- ★ There is a lot of work to find the right stocks
- ★ And even hard work does not guarantee success



### 3. Do you have the knowledge?

- ★ If you are interested and have the time, but you know nothing about investing, it's a problem

### 3. Do you have the knowledge?

- ★ You cannot just go into the stock market and expect to win when you have no idea of what you are doing

### 3. Do you have the knowledge?

- ★ Do you have 10 to 20 extra hours a week to devote to learning about picking stocks?



# What if your answer is “Yes”?

- ★ For those who answer “Yes” that you have interest, time, and knowledge
  - Managing your own portfolio of stocks can be fun, challenging, and rewarding

# What if your answer is “Yes”?

- ★ There are some advantages to an individual picking stocks

# What if your answer is “Yes”?

- ★ But if you have made it this far in this course, I will assume you answered “No” to most, if not all those questions



# If you answered “No”

- ★ Let's consider your first option
  - A mutual fund

# A mutual fund

- ★ A stock mutual fund is a legal entity into which individuals add their money
- ★ Then a fund manager decides what stocks to buy with that money

# A mutual fund

- ★ It allows one small shareholder to own a tiny slice of many stocks



# An actively managed mutual fund

- ★ Most mutual funds in the world are actively managed

# An actively managed mutual fund

- ★ A fund manager actively attempts to pick stocks that she thinks will beat the market
  - Warren Buffett is one of the most well-known active fund managers

# An actively managed mutual fund

- ★ The objective of an active fund manager is to beat the market

# An actively managed mutual fund

- ★ To try to do this the fund manager will usually find and hold good stocks that are reasonably priced

# An actively managed mutual fund

- ★ The good news is when you invest with an active fund manager, because the fund owns many stocks, you reduce unnecessary company-specific risk

# An actively managed mutual fund

- ★ But there is one problem, it's hard to find an active fund manager who can consistently beat the market



# An actively managed mutual fund

- ★ In fact, it is very, very difficult to find that winning fund manager,
  - Before she is a winning fund manager,

# An actively managed mutual fund

- ★ Unless you happen to meet by chance

# Here's someone who did win by luck

## In 1965, This Man Asked His Neighbor – Warren Buffett – To Manage His Life Savings. Guess How That Turned Out

By Brian Warner on January 30, 2017 in Articles > Entertainment

In the mid 1960s, a husband and wife named Dorothy and Myer Kripke faced a difficult problem. A problem that is fairly common for many middle-aged couples. How do you properly plan for retirement? Dorothy and Myer were actually way ahead of most of their peers when it came to retirement planning. Thanks to diligent saving habits and a small inheritance, by 1965 they had managed to sock away roughly **\$67,000**, which is equal to roughly \$500,000 today after adjusting for inflation. That was the good news. The bad news was that they now needed to protect and grow the savings so it would still be there when they were ready to retire in a decade or two. After months of stressful debating, Dorothy offered her husband some simple advice:

**"Myer, invest the money with your friend, Warren."**

Steps    1   2   3   4   **5**   6   7   8   9   10   11   12



- ★ This couple, by chance, lived next to Warren Buffett
- ★ They gave Warren \$67,000 in 1965 and it grew to be \$40 million by 1995

# What can research teach us?

- ★ In the world of finance, one surprising thing is that the more you pay, often the less you get

**Research**



# What can research teach us?

- ★ In 2018 there were 118,978 regulated funds
  - 47% in Europe
  - 28% in Asia-Pacific region
  - 8% in the United States
  - 17% in the rest of the world

**Research**



# What can research teach us?

- ★ 34% were equity funds
- ★ 18% were bond funds
  - 46% were mixed/other funds
  - 2% were money market funds

**Research**





# What can research teach us?

- ★ In 2018 there was \$18 trillion of assets in the US mutual fund industry, broken down as follows

**Research**



# What can research teach us?

- ★ 52% equity mutual funds
- ★ 23% bond mutual funds
- ★ 17% money market funds

**Research**



# The number of funds in the world

Region	2013	2014	2015	2016	2017	2018
Americas	23	25	26	26	27	28
Europe	52	52	53	54	55	56
Asia Pacific	21	24	27	29	30	33
Other	1	1	1	2	2	2
World	98	102	107	111	114	119

**Research**



# Countries and funds

Country	2013	2014	2015	2016	2017	2018
Luxembourg	14	14	14	14	15	15
Korea	10	11	12	13	12	13
Japan	8	9	10	11	12	12
France	11	11	11	11	11	11
Brazil	8	9	9	9	10	10
United States	9	9	10	10	10	10
Ireland	6	6	6	6	7	7
Germany	6	6	6	6	6	6
China	1	2	3	4	4	5
Canada	3	4	4	4	4	4
United Kingdom	2	3	3	3	3	3
Other	20	19	20	21	21	22
<b>World</b>	<b>98</b>	<b>102</b>	<b>107</b>	<b>111</b>	<b>114</b>	<b>119</b>

## Research



# What can research teach us?

- ★ About 80% of mutual funds are actively managed
- ★ Together, all those funds are managing almost 25 trillion dollars

**Research**



# What can research teach us?

- ★ The problem is that
- ★ Many academic studies looking at the performance of fund managers have concluded

**Research**





# What can research teach us?

- ★ That most actively managed funds do not beat the market

**Research**



# Why do active funds underperform?

- ★ They certainly are paid well to pick the right stocks!

**Research**



# Why do active funds underperform?

- ★ Often that is the very reason they underperform

**Research**



# Why do active funds underperform?

- ★ The return that you, the investor, receives is always after the fund manager's fees

**Research**



# Why do active funds underperform?

- ★ If your fund manager can generate an annual 10% return, but his fees are 2%,

**Research**



# Why do active funds underperform?

- ★ Then you, the investor, only receive an 8% return

**Research**





# Why do active funds underperform?

- ★ The higher the fees, the harder it is for you to get a high return from an active fund manager

**Research**



# Why do active funds underperform?

- ★ Besides fees, another reason that active fund managers have a hard time outperforming is that the stock market is incredibly complex

**Research**



# Why do active funds underperform?

- ★ Over and over it has been shown that no one can consistently predict the stock market

**Research**



# Low chance of finding the winning fund manager

- ★ The famous champion of the average investor, John Bogle, wrote the seminal “The Little Book of Common Sense Investing”

**Research**



# Low chance of finding the winning fund manager



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**Research**



# Low chance of finding the winning fund manager

- ★ In it, he looked at 355 mutual funds that existed in 1970 and determined how many of them actually beat the stock market over the following 35 years

**Research**



# Low chance of finding the winning fund manager

- ★ What he found was that about 24 funds managed to outperform over that time period

**Research**



# Low chance of finding the winning fund manager

- ★ This means that an investor in 1970 had only a 7% chance that they would pick a mutual fund that outperformed over the long run

**Research**





# Low chance of finding the winning fund manager

- ★ So trying to pick the winner before she is the winner is a bad way of thinking about investing

**Research**



# Don't base your financial future on luck

- ★ Luckily, there is another option for the average investor who does not want to invest in an actively managed fund

# Don't base your financial future on luck

- ★ A passively managed fund

# A passively managed mutual fund

- ★ A “passively managed index fund” is sometimes just called a “passively managed fund”

# A passively managed mutual fund

- ★ Objective of a passively managed fund is to match the stock market index performance, not beat it

# A passively managed mutual fund

- ★ These funds do not make bets on individual stocks or sectors, nor do they try to time the market, because they are not trying to outperform it

# A passively managed mutual fund

- ★ Most passive funds are also called index funds, meaning that they are trying to just match the stock market index

# A passively managed mutual fund

- ★ The benefit of passively managed funds is that they are low-cost, unlike actively managed funds



# A passively managed mutual fund

- ★ Their downside is that they are not “sexy”
- ★ They are never going to beat the market, because they are the market

# Passive funds have long-term benefits

- ★ Most people should invest their money in a passively managed index fund. Why?

# Passive funds have long-term benefits

- ★ If financial independence is your goal, its probably better to focus on building your wealth through business, and then investing that in a passively managed index fund

# Passive funds have long-term benefits

- ★ Rather than investing substantial time, and then hoping your stocks or your active fund succeed

# Three ways to invest in the stock market

- ★ Now you know three ways you can invest in the stock market and take your finances into your own hands

# Three ways to invest in the stock market

- ★ 1. Own and manage your own portfolio of no less than 10 stocks
  - Problem: Complicated and time consuming


# Three ways to invest in the stock market

- ★ 2. Own an actively managed fund run by a fund manager who you think is going to beat the market
  - Problem: Hard to find, expensive, and probably won't outperform over the long run

# Three ways to invest in the stock market

- ★ 3. You could own a passively managed index fund that matches the market
  - Problem: You will never “outperform” the stock market
  - For most people this is the right choice






What you  
have  
learned

- Most mutual funds are actively managed, they are constantly trying to beat the market





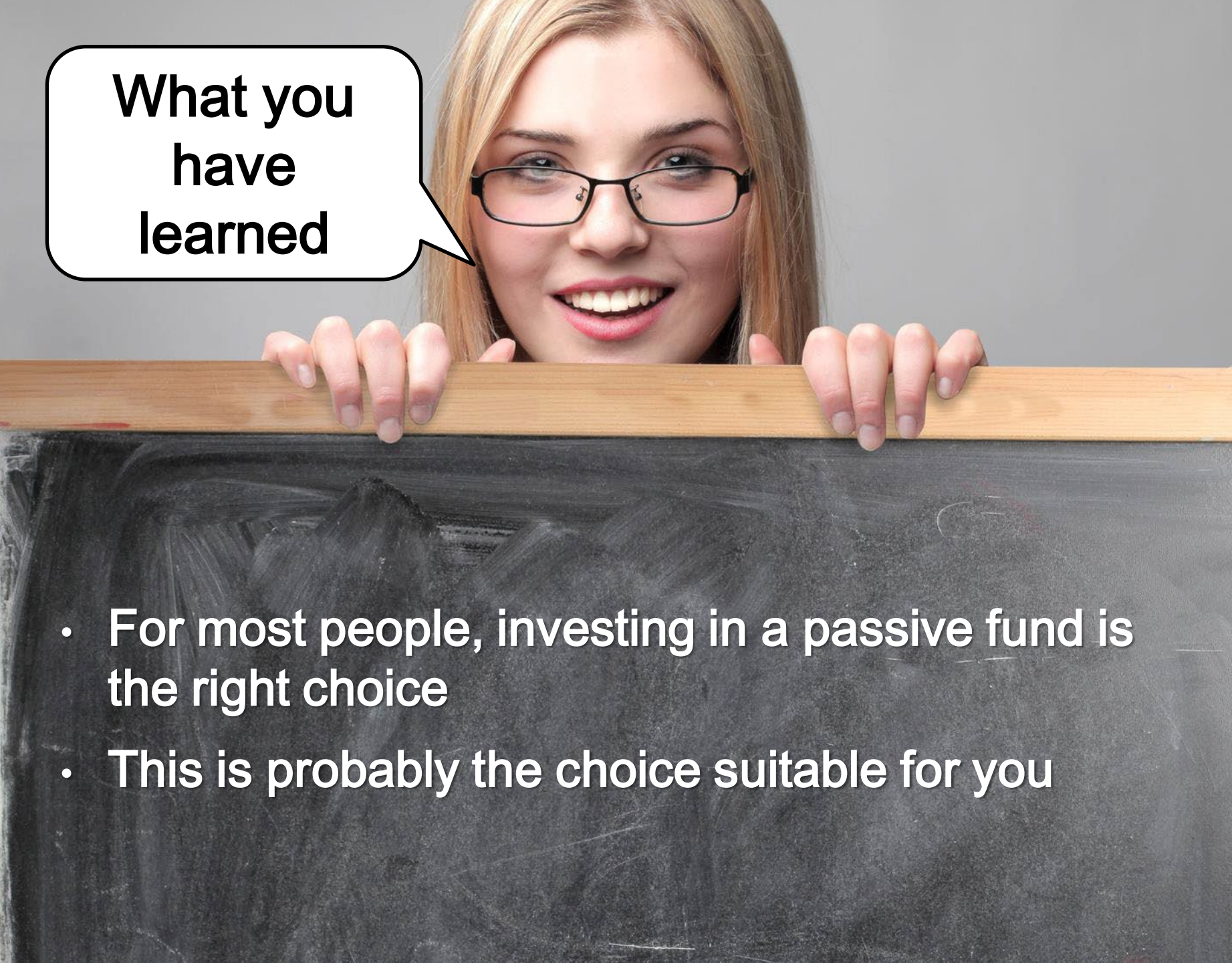
What you  
have  
learned

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- But, most actively managed funds do not beat the market






What you  
have  
learned

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- Your chance of finding a consistently winning active fund manager before they have their winning streak is very low






What you  
have  
learned

- The alternative to an actively managed fund is a passively managed index fund

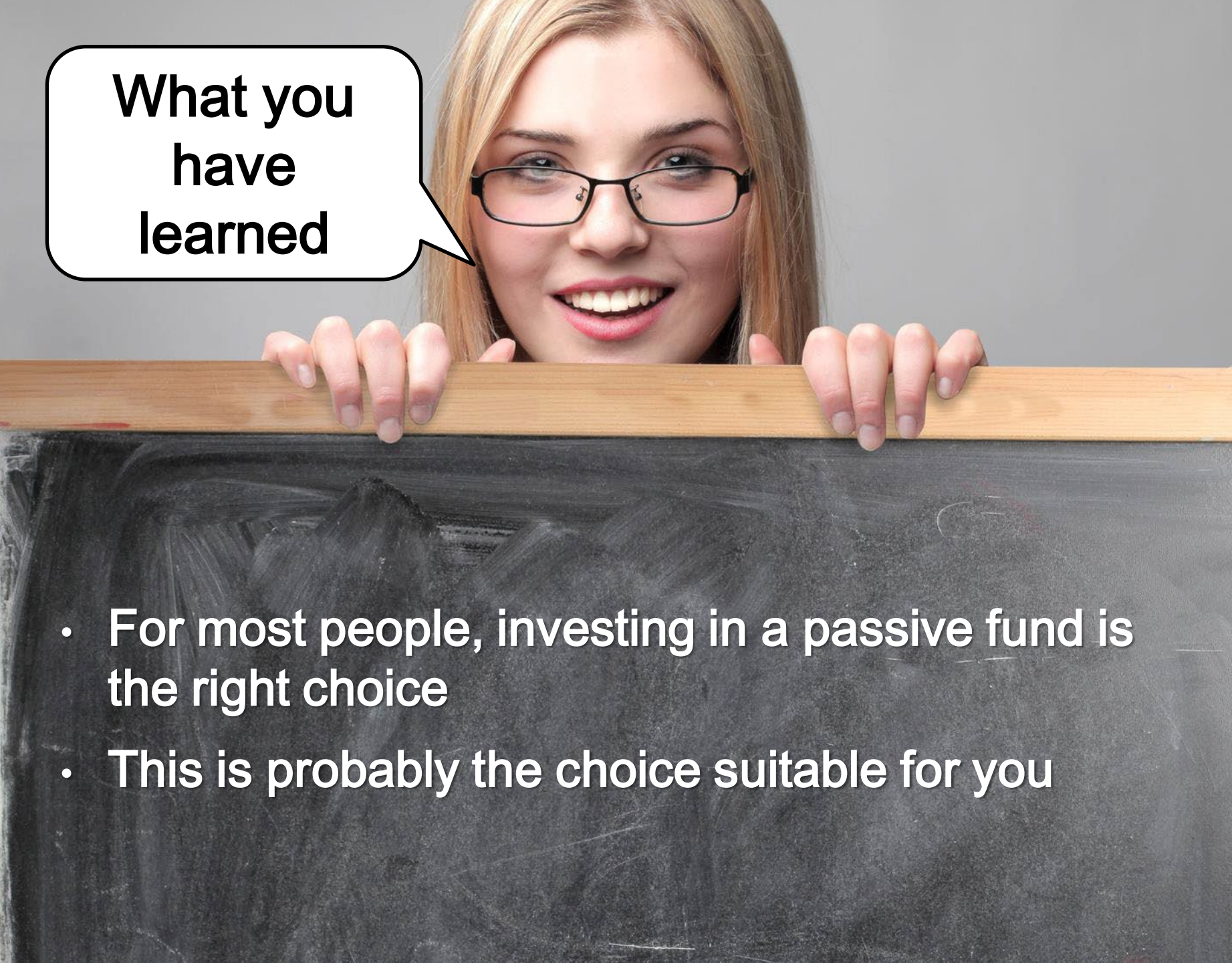




What you  
have  
learned

- Passive funds buys all the stocks in a specific market and aims only to match that market, not beat it



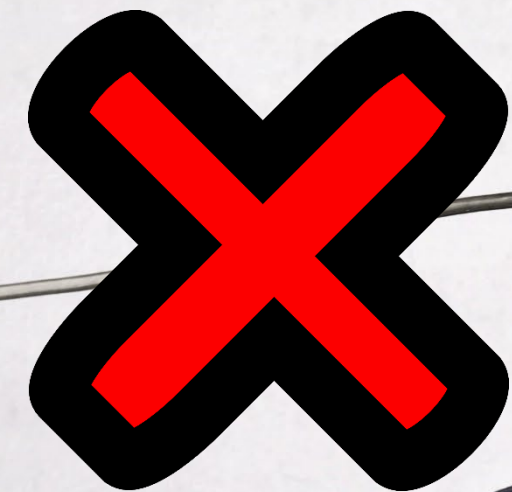


What you  
have  
learned

- For most people, investing in a passive fund is the right choice
- This is probably the choice suitable for you



**Rely on others too  
much**



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