

Canadian Financial DIY

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Tuesday, 23 February 2010

The Myth that ETFs are Always and Necessarily Better than Mutual Funds

It's all about costs and investment strategy. Whether a fund is an ETF or a mutual fund doesn't matter all that much. If the costs to buy into, to manage and to run the fund are low and it passively invests in a broad market index, the results for the retail individual investor will be good. The fact that mutual fund fees in Canada have been high and net investor returns have been low as a consequence does not mean it has to be so. In fact, ETFs are catching up to mutual funds in both good and bad ways. The recent proliferation of new ETFs with active trading strategies, narrow asset groupings and leveraging, foretell that investor returns will be poor.

That it is possible for mutual funds to equal the original virtues of ETFs is evident at the US fund company [Vanguard](#), which offers both ETFs and mutual funds.

Here is a sample of funds with identical holdings and thus returns, apart from fees. In fact, the ETFs of Vanguard are merely a share class of the same asset base.

- US Total Stock Market ETF (symbol: VTI) - MER 0.09%
- US Total Stock Market Index Fund (VTSMX) - MER 0.18%
no purchase or redemption fee

- US total Bond Market ETF (BND) - MER 0.14%
- US Total Bond Market Index Fund (VBMFX) - MER 0.22%
no purchase or redemption fee


- Emerging Markets ETF (VWO) - MER 0.27%
- Emerging Markets Fund (VEIEX) - MER 0.39% plus
purchase fee 0.50% and redemption fee 0.25%

The mutual fund on-going MER fees are a bit higher but for someone trying to make regular small purchases through an automatic savings and investment plan, avoiding the payment of trading commissions on ETFs, even when they are \$10 per trade from a discount broker (a \$10 cost on a \$1000 purchase is a 1% "fee") makes the two alternatives very similar. Add in the convenience of automatic dividend reinvesting (DRIP) and tax record keeping that mutual funds offer, and ETFs lose their advantage. Vanguard even has a handy [ETF vs mutual fund calculator](#) to compare which version you would be better off to

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Fundamental vs Cap-Weight Portfolios

main etf portfolio_v3b

Total Portfolio at Start C\$100,000							
Fundamentally-Weighted Portfolio				Market Value			
Security	Ticker	# of Shares	Price / Share	US\$ Value	Market Value C\$	Diff Fund minus Cap	
Claymore Cdn Fundamental Index	CRQ	1252	10.98		13747	-\$19	IUNITS S&P/TS
iShares TSX Mid-cap	XMD	216	18.89		4080	\$0	iShares TSX M
BMO Equal Weight REITs Index	ZRE	134	16.15		2164	\$16	iShares Cdn R
iShares DEX Universe Bond Index Fund	XBB	844	29.98		25303	\$0	iShares DEX U Fund
BMO Real Return Bond Index	ZRR	667	15.13		10092	\$0	BMO Real Ret
PowerShares FTSE™ RAFI US 1000 Portfolio	PRF	141	47.76	6734	7051	\$35	Vanguard Larg
PowerShares FTSE RAFI US 1500 Small-Mid Portfolio	PRFZ	75	50.22	3767	3944	\$37	Vanguard Sma
PowerShares FTSE RAFI Emerging Markets Portfolio	PXH	232	21.99	5102	5342	-\$107	Vanguard Eme
PowerShares FTSE RAFI Developed Markets ex-U.S. Portfolio	PXF	572	34.83	19923	20859	\$295	Vanguard FTSE
PowerShares FTSE RAFI Developed Markets ex-U.S. Small-Mid Portfolio	PDN	201	20.38	4096	4289	-\$5	iShares MSCI I
SPDR DJ Wilshire International Real Estate	RWX	60	34.6	2076	2174	-\$36	SPDR DJ Wils
iPath DJ-AIG Commodity Index Total Return	DJP	102	40.02	4082	4274	\$0	iPath DJ-AIG C
Total Portfolio					\$103,318	\$216	Total Portfolio
Cash					\$516		Cash
Portfolio Net including Cash						\$168	
			Approx C\$ per US\$	1.047010784			

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