

26. Mutual Funds 5: Fees: Load and No-load etc.

Load and no-load fees

Expense ratios

Actively and passively managed mutual funds

Terminology – mostly U.S.

Minimize fees and only paying for fees that actually add value

Concepts can be usually applied

Load fees are like a commission that can be charged on purchase or redemption of the funds

Distribution fees - US – 12B1 fees

Load fees are commission fees that go to the broker for selling mutual funds to the investor

Front-end fees (bought) / back-end fees (funds sold) – are also known as redemption fees

Not paying a load fee at the outset or on redemption is much better

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At the outset we lose money

Avoiding the load fees is a very good idea

A “no-load” fund doesn’t mean it’s free of charges

A no-load fund still charges distribution fees

And a no-load fund that doesn’t charge distribution fees is also known as a 100% no-load fund

But they still charge the 12B1 fee – so watch out for that

US equity fund or mutual fund benchmarked to the S&P 500 will have “no-load” funds as an alternative

To run mutual funds, there are operating expenses passed on to the investor

Distribution, portfolio or management, trade, research, holding securities, and other admin. fees

They eat into the net performance of fund

Analyzing securities, there is a lot of debate about whether active management – question whether it actually adds value

And whether net performance of an active management outperforms a passive strategy that attempts to mirror the index and has lower expenses

Books argue that passive management in mature markets is definitely the way to go

In active management going to justify the incremental fees. Studies show that the manager is not able to pick the under valued portfolios consistently

The active management doesn’t outperform the benchmark on a net basis or the lowest expense ratio tends to be for passively managed funds, that the expense ratio expresses a percentage and is annual percentage that an investor pays for the mutual fund separate from the load and no-load matter

If we look at expense ratio of a fund, it gives us an indication of what the costs are, excluding the load and no-load matters.

No-load fund – what the costs are on a percentage basis

Load funds will also show gross performance – i.e., before any charges and performance on a net basis

Looking at these charges is crucial to understand how the fund really performed

There are a lot of reasons, including market efficiency, to look at passively managed funds, but also aims to avoid the load charges

Expense ratios that can have an impact on net performance, especially when were compounding a different interest ratio

Compounding at 3% or at 3.5% over a very long period makes a difference of end result over 10 or 15 years of much greater than .5%

If the percentage return on a net basis makes a big difference

Look at tax implications as well

The question is, will active management will up from the benchmark – a lot of debate, especially in a very mature market