

selecting mutual funds

How do I select a fund that's right for me?

There are a number of steps to take to determine which fund is right for you.

Goals

With the help of an investment advisor, or on your own, start the process by determining your goals. If you want to keep your money safe and earn a little interest at the same time, a less risky money market fund may do the job nicely. But if you're trying to build substantial savings for a long-term goal, such as retirement, a money market fund probably wouldn't be the best choice.

You'll need to consider increasing the risk of your portfolio to better your chances of earning more.

Risk

The next step is to determine how much risk you can tolerate. Part of figuring out your risk tolerance is the sleep test. If you have trouble sleeping at night because you're worried about how your mutual funds are doing, you're probably taking on too much risk. The risks involved in buying a particular fund are described in the mutual fund's simplified prospectus, and an investment advisor can help you determine your risk level.

Time Horizon

Another key consideration is the length of time you have to save. If you are saving for a retirement that is still 30 years off, you can afford to take a greater amount of risk.

If you have three decades, the ups and downs of the stock market should not be such a great concern. Some of your riskier investments could drop in the short term, but over the longer term, past experience suggests that a broadly diversified portfolio of stock investments tends to rise more often than it drops. However, if you only have a small window of time before you'll need your money, or if you are saving for a short-term goal, you should consider reducing your risk. In this case, there isn't enough time left for your investments to recover should they drop in value.

Factors to Consider

When choosing a specific fund that matches your objectives, risk tolerance level and time horizon, there are a number of factors to consider:

Goals. Ensure that the fund's objectives and goals match your own.

Performance. While past performance doesn't guarantee future returns, looking at both long term and short term past performance can give you an idea of what the fund has been capable of. It is also wise to look at individual year returns as well as compound annual returns. If a fund's returns swing widely from year to year, they may affect your sleep factor.

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Factors to Consider (cont'd)

Management. How long has the fund's management team been in place? And what is the manager's track record?

Fees. Fees vary greatly and it is up to you to decide if you want to pay loads in return for advice or buy direct. Compare management expense ratios within the same type of fund group to analyze if the fund's fees are in the appropriate range for that type of fund.

Service. What type of service will you be receiving with the fund you choose?

Source: Investment Funds Institute of Canada