Mutual Fund Observer

“The journey of a thousand miles begins …

… with one step.” Lao-Tzu.

A Guide to Investing In Your First Mutual Fund

Good news: you’re ready to take that step and we’re here to help make it happen. We’re going to guide you through the process of setting up your first investment account. There are only two things you need to know:

It’s easy and
It will make a *big* difference. You’ll be glad you did it.

It’s easy. A mutual fund is simply a way of sharing with others in the costs of hiring a professional to make investments on your behalf. Mostly your manager will invest in either stocks or bonds. Stocks give you part-ownership in a company (Apple, Google, Ford); if the value of the company rises, the value of your shares will rise too. Some companies will soar; others will crash so it’s wiser for investors to invest broadly in a bunch of companies than to try to find individual winners. Bonds are ways for governments or companies to borrow money and pay it back, with interest, over time. “Iffy” borrowers have to pay a bit more in interest, so you earn a bit more on loans to them; high quality borrowers pay you a bit less but you can be pretty sure that they’ll repay their borrowings promptly and fully.

Over very long periods, stocks *make* more money than bonds but, over shorter periods, stocks can *lose* a lot more money than bonds. Your best path is to own some of each, rather than betting entirely on one or the other. If you look back over the last 65 years, you can see the pattern: stocks provide the most long-term gain but also the greatest short-term pain.

Average performance, 1949-2013	80% stocks / 20% bonds & cash	60% stocks / 40% bonds & cash	40% stocks / 60% bonds & cash
Average annual gain	10.5%	9.3	8.1
How often did it lose money?	14 times	12 times	11 times
How much did it lose in bad years?	8.8%	6.4%	3.0%
How much did it lose in its worst year?	28.7%	20.4%	11.5%

How do you read the table? As you double your exposure to stocks, going from 40% to 80%, you add 2.4% to your average annual return. That's good, though the gain is not huge. At the same time, you increase by 30% the chance of finishing a year in the red and you triple the size of the loss you might expect.

We searched through about 7000 mutual funds on your behalf, looking for really good first funds. We looked for four virtues:

- **They can handle stormy weather.** All investments rise and fall; we found ones that won't fall far and long.
- **They can handle sunny weather.** Over time, things get better. The world's economy grows, people have better lives and the world's a richer place. We found funds that earned good returns over time so you could benefit from that growth.
- **They don't overcharge you.** Your mutual fund is a business with bills to pay; as a shareholder in the fund you help pay those bills. Paying under 1% a year is reasonable. While 1% doesn't seem like a lot, if your fund only makes 6% gains, you'd be returning 17% of those profits to the manager.
- **They require only a small investment to get started.** As low as $50 a month seemed within reach of folks who were determined to get started.

Getting the account set up requires about 20 minutes, a two page form and knowing your checking account numbers.

It will make a difference. How much can $50 a month get you? In one year, not so much. Over time, a surprising lot. Here's how much your account might grow using three pretty conservative rates of return (5-7% per year) and four holding periods.

	5%	6%	7%
One year	$ 667	670	673
Ten years	7,850	8,284	8,750
Twenty years	20,700	23,268	26,250
Forty years	76,670	100,120	$ 132,100

You read that correctly: if you're a young investor able to put $50 a month away between now and retirement, just that contribution might translate to $100,000 or more.

Two things to remember: (1) **patience is your ally**. Markets can be scary; sometimes they're going down and you think they'll never go up again. But they do. Always have. Here's how to win: set up your account with a small automatic monthly investment, check in on it every year or so, add a bit more as your finances improve and go enjoy your life. (2) **Small things add up over time**. In the example above, if your fund pays you just 1% more it makes a 30% difference in how much you'll have over the long term. Buying a fund with low expenses can make that 1% difference all by itself, and so can a small increase in the percentage of your account invested in stocks.

Three funds to consider. The August 2015 issue of Mutual Fund Observer, available free on-line at www.mutualfundobserver.com, provides a more complete discussion of each of these funds. In addition to our own explanation of them, we've provided links to the form you'd need to complete to open an account, the most recent fact sheet provided by the fund company (it's a two page "highlights of our fund" document) and a link to the fund's homepage.

James Balanced: Golden Rainbow (ticker symbol: GLRBX). The fund invests about half of its money in stocks and half in bonds, though the managers have the ability to become much more cautious or much more daring if the situation calls for it. Mostly they've been cautious, successful investors; they've made about 6.9% per year over the past decade, with less risk than their peers. During the very bad period in 2008, the stock market fell about 40% while Golden Rainbow lost less than 6%. The fund's operating expenses average 1.01% per year, which is low. Starting an account requires a monthly investment of $500 or a one-time investment of $2,000.

Why consider it? Very low starting investment, very cautious managers, very solid returns.

Profile | Fact Sheet | Application

TIAA-CREF Lifestyle Conservative (TSCLX). TIAA-CREF's traditional business has been providing low cost, conservatively managed investment accounts for people working at hospitals, universities and other non-profit organizations. Today they manage about $630 billion for investors. The Lifestyle Conservative Fund invests about 40% of its money in stocks and 60% in bonds. It does that by investing in other TIAA-CREF mutual funds that specialize in different parts of the stock or bond market. This fund has only been around for four years but most of the funds in which it invests have long, solid records. The fund's operating expenses average 0.87% per year, well below average. Starting an account requires a monthly investment of $100 or a one-time investment of $2,500.

Why consider it? The most conservative stock-bond mix in the group, solid lineup of funds it invests in, low expenses and a rock-solid advisor.

Profile | Fact Sheet | Application

Vanguard STAR (VGSTX). Vanguard has a unique corporate structure; it's owned by the shareholders in its funds. As a result, it has been famous for keeping its expenses amazingly low and its standards consistently high. They now manage over $3 trillion, which represents a powerful vote of confidence on the part of millions of investors. STAR is designed to be Vanguard's first fund for beginning investors. STAR invests about 60% of its money in stocks and 40% in bonds. It does that by investing in other Vanguard funds. Over the past 10 years, it has earned about 6.8% per year and it lost 25% in 2008. The fund's operating expenses are 0.34% per year, which is *very* low. Starting an account requires a one-time investment of $1,000.

Why consider it? The lowest expenses in the group, one-stop access to many of the best funds offered by the firm many consider the best in the world.

Profile | Fact Sheet | Application

Manning & Napier Pro-Blend Conservative Term (EXDAX). Manning & Napier was founded in 1970 by two guys who were very consciously concerned with putting shareholders first. That meant not losing money. It has maintained that culture and now manages more than $42 billion for clients large and small.

EXDAX is designed to be a core holding for conservative investors. It's emphasis is on avoiding losses, first and foremost, then exploiting whatever opportunities the market might reasonably offer. It invests about 70% of its money in bonds and 30% in stocks. Over the past 10 years, it has earned about 5.1% per year and it lost 5% in 2008. The fund's operating expenses are 0.87% per year, which is *reasonably* low. Starting an account requires a one-time investment of $2,000 or an ongoing automatic investment of $25/month.

Why consider it? EXDAX may not excite you, but it's also not likely to frighten or disappoint you. It should produce solid, inflation-beating returns in good markets and bad. While it won't rush to the head of the pack, it should exemplify the virtues of "slow and steady."

Profile **Fact Sheet** **Application**

We're targeting funds for you whose portfolios are somewhere around 40-60% stocks. Why so cautious? You might be thinking, "hey, these are Old People funds! I'm young. I've got time. I want to invest in stocks, exciting 3D printing stocks!" Owning too many stocks is bad for your financial health. Imagine that you were really good, invested steadily and built a $10,000 portfolio. How would you feel if someone broke in, stole $5,000 from it and the police said that they thought it might take five to ten years to solve the crime and get your money back? In the meantime, you were out of luck. That's essentially what happens from time to time in the stock market and it's really discouraging. Those 3D printing stocks that seem so exciting? They've lost two-thirds of their value in the past year, many will never recover.

If you balance your portfolio, you get much better odds of success. Remember Table One, which gives you the tradeoff? Balancing gives you a really good bargain, especially for the first step in your journey.

So what's the next step? It's easy. Pick the one that makes the most sense to you. Take 20 minutes to fill out a short account set-up form online. Tell them if you want to start by investing a little money or a lot. Fill it out, choose the option that says "reinvest my gains, please!" and go back to doing the stuff you really enjoy.

Contact us:

Mutual Fund Observer, Inc.
5456 Marquette Street
Davenport, IA 52806

www.mutualfundobserver.com