

Exchange Traded Funds vs Mutual Funds

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Most investors are aware of what a mutual fund is, but there is less general understanding about what an exchange traded fund (ETF) is. Much of the discrepancy can be explained by the fact that mutual funds have been around for more than 50 years longer than ETFs which were introduced a little over two decades ago. Mutual Funds and ETFs essentially compete against each other for attracting investor assets and with 50+ years of seniority, mutual funds hold a decisive edge in terms of number of products and total assets under management.

The purpose of this report is to illustrate the similarities and differences between mutual funds and ETFs both descriptively and with summaries in a table format. We will also show an example that compares a mutual fund and an ETF with similar investment criteria.

Mutual Funds:

A mutual fund is an investment vehicle owned by many investors who pool their capital together for the purpose of investing in securities such as stocks, bonds, and other assets. Mutual funds are managed by professional money managers, who invest the fund's capital and attempt to produce capital gains and income for the fund's investors. A mutual fund's portfolio is managed in accordance with the investment objectives stated in its prospectus.

Mutual funds are typically sold or recommended by licensed representatives of financial institutions or investment dealers, as well as directly through the mutual fund companies. Mutual funds are bought and sold at the Net Asset Value (NAV) price established at the end of every trading day by taking the

closing values of each investment and dividing by the number of outstanding units or shares.

Most mutual funds are actively managed which means that they seek to generate an investment return that is better than the return of the fund's benchmark. Benchmarks are typically representative indices such as the S&P/TSX Composite or S&P 500, or combinations of indices, depending on what is defined by its investment objectives.

Exchange Traded Funds:

Like the name suggests, an ETF is a fund that trades on an exchange, such as the Toronto Stock Exchange. Similar to a mutual fund, an ETF typically owns a number of underlying assets, such as stocks or bonds, and shares are issued to investors for a pro-rata representative ownership.

ETFs are purchased very similarly to how shares in common equity are purchased. Any investor who has a brokerage account may purchase ETFs and will pay a transaction charge whether it is purchased directly by the investor or through a financial representative. The price of the ETF will be determined by supply and demand, but generally will trade very close to its NAV.

A major distinction between most ETFs and mutual funds is that ETFs attempt to replicate the performance of its underlying benchmark, rather than to try and beat it. Since the composition of benchmarks are readily available, it is relatively easy task to administer, and therefore providers of ETFs charge very low management expense ratios (MERs). This is in contrast to mutual funds which charge relatively large fees since they attempt to "outsmart" these similar benchmarks.

	Mutual Funds	ETFs
Diversified Holdings?	Yes	Yes
Trading	Purchased through Mutual Fund company or dealer at daily NAV	Purchased on a stock exchange at prevailing market prices
Performance Objective	Attempts to beat the benchmark	Attempts to match the benchmark
Fees	High MER	Low MER
Transaction Costs	May contain purchase or redemption charges	Brokerage commission

As an example between a mutual fund and a comparable ETF, we took the oldest mutual fund and oldest ETF that use the S&P/TSX Composite as their benchmark. According to data from

Morningstar Direct and the respective websites of the manufacturer of each fund, we present the following as of October 31st, 2017:

	Desjardins Canadian Equity Growth Mutual Fund	iShares Core S&P/TSX Capped Composite Index ETF
Inception Date	October 30, 1956	February 16, 2001
Benchmark	S&P/TSX Composite Index	S&P/TSX Composite Index
Number of Holdings	118	249
Most recent MER (Fees)	2.37%	0.06%
10-Year Performance (Annualized)	1.36%	3.77%

Sources: Morningstar Direct, Desjardins Funds, Blackrock

It should be noted that over time, MERs can change, fund managers can change, and benchmarks can change so further analysis may be required to draw any conclusions. In general terms, however, these results are typical of research studies that show after fees, ETFs provide a compelling alternative to mutual

funds due to the significantly lower fees charged, particularly over longer periods of time.

*** Full Disclosure: Justwealth holds the iShares Core S&P/TSX Capped Composite Index ETF in a number of our portfolios*



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