CHEAPEST WAY TO BUY ETF'S

BLOEMFONTEIN: I have been a staunch advocate of Exchange Traded Funds (ETF's) from the launch of the first ETF in November 2000. Since then, many new indexed products have been launched and various companies have created new options for purchasing these investments. As a result, I have been getting an increasing number of questions from readers asking me how they should buy these indexed investments. The variety of purchasing options available to investors makes the answer quite complicated. To that end, I am very grateful to one of our regular readers, Hercules Viljoen from Pretoria for sending me his research on the cheapest way to purchase ETF's. I wish more people would take the time to share their research so that we can all benefit and the best product providers get the most support.

FEEDBACK FROM A READER

Hercules (who does not work in the investment industry) has taken the time to analyse the cheapest way for an individual to buy ETF's. More specifically he has analysed the impact of the purchase costs for different amounts of money e.g. R500, R1,000 or R10,000. He was adamant that I remind people that this is his own research and investors should still do their homework before investing their money.

RANGE OF OPTIONS

You can currently buy ETF's via two main platforms, either directly from an ETF promoter e.g. www.etfsa.co.za or www.satrix.co.za or via a stock broker. What makes the cost comparison complicated is that some stock brokers have different pricing structures for different investments. In addition, these costs do change regularly. One aspect of Viljoen's research that I really like is that he has incorporated the cost of selling your investment after a 10 year period to make the comparisons realistic. This is important because it means we can see the cost of buying, holding and selling the ETF's which is what most of us will do with these investments over time.

My understanding of Viljoen's research shows that buying ETF's directly from an ETF promoter is your best option for smaller amounts e.g. from R300 to R1,000 per month. The transaction costs are lowest and your holding costs are not too high in comparison to a stock broking account where they normally charge a fixed fee and not a percentage fee. If you are investing larger sums e.g. from R1,000 to R8,000 per month, a stock broking account using one of their special pricing packages might work best. Some stock brokers like Standard Bank and FNB Online offer reduced trading costs if you trade specific shares or ETF's. These are the more tradable (liquid) shares on the JSE and are specified by these brokers on their websites. For larger transaction amounts (over R8,000) the picture becomes quite murky indeed. Typically, your best cost for large transactions (over R10,000) will probably be a normal stock broker and can be negotiated.

As Viljoen points out, the bulk of South African, middle income earners will probably be investing between R1,000 and R8,000 per month and this means the specialist trading packages from the stock brokers are the lowest cost option. This is especially true if you invest this money on a monthly basis over a long period of time because your annual holding costs will reduce as your investment grows in size. With the direct ETF promoters, your annual holding costs also reduce as your investment grows but not by the same extent as the online brokers. Viljoen personally prefers the Standard Bank option called ASI but he says FNB Sharebuilder product comes a close second. If you would like to see Viljoen's detailed model you can find it here.

BELOW R300 IS PROBLEMATIC

For the past few months I have been doing some extensive research into low cost savings options for people who can only afford amounts of R50 – R300 per month. Sadly most of the investments that accept small amounts on a monthly basis are actually quite expensive (in percentage terms) to the extent that your growth is usually eroded by costs. Sadly even the government RSA Retail Savings Bonds do not cater for monthly investments. This means your best option for smaller amounts is probably to save the money in a money market account and then to do quarterly or half-yearly payments into a higher growth savings option like an ETF. There are some interesting service providers who are investigating how they can use their existing infrastructure to offer low cost savings vehicles for smaller investors.

CONCLUSION

The current market conditions have been wonderful for people who are saving on a monthly basis. The dramatic volatility has offered quite a few opportunities to buy great investments at ridiculously low prices. For those of you who should be saving on a monthly basis and are not doing so now; make a start as soon as possible. There is no guarantee that the market will continue to offer such good value so you need to climb in now. Don’t worry about all the roller coaster movements that we are seeing now, this is good for savers so take advantage.