# CHOOSING UNIT TRUSTS – NOT AN EASY TASK

I have worked in the private client investment industry for nearly two decades and have always been involved in selecting shares, unit trusts, ETF's and other investments for my clients. Part of my career was spent working for one of SA's largest private client stockbrokers where I was the designated unit trust selector. So in December last year, when financial journalist Bruce Whitfield, challenged me on live radio to select my five best and five worst unit trusts for 2013, you would think that I would have been pretty confident of doing a good job. You would have been mistaken; in fact, I was trying desperately to find a way out of his challenge because I knew my chances of failure were much greater than my chances of success. The reason? More than 70% of unit trust managers can't beat the stock market over long periods of time. Even great fund managers have long periods where they underperform. So trying to select funds over a 12-month period was always going to be a matter of luck rather than skill.

Unsurprisingly, my "best" funds are currently not beating my "worst" funds. Fortunately, my default choice (investing in the index instead) has been the best choice by far. While my ego is bruised, I am at least comforted that my long-held faith in indexation is being vindicated at this time. This experience also reinforces how difficult it is for private investors to select unit trusts for themselves. If most unit trusts underperform the index over the long-term, one could be forgiven for simply choosing the biggest and oldest funds. Alternatively, one could select the "rock stars" of the fund management industry in the hope that they will replicate their past success. Sadly this could be a big mistake too. One of the managers I selected for 2013 is John Biccard who manages the Investec Value fund and this has been my worst performer so far. Biccard is one of SA's best money managers, he has a great track record and has a rigid "value" philosophy when it comes to selecting individual shares. The fact that he is not shooting the lights out right now does not worry me but it does illustrate my point about short-term underperformance.

Two well-respected American finance professors, Gary E. Porter and Jack W. Trifts, studied fund manager performance over long periods of time and came to some interesting conclusions. Fund managers who have been in the job for more than 10 years are likely to deliver deteriorating performance the longer they remain in charge. These are the same managers who would have delivered great returns in their first three years as fund managers. So, we cannot simply rely on a fund manager's track record when making a fund selection decision. The task of choosing a good fund is so difficult that Professor Porter, concluded: "we caution investors to avoid actively managed funds. We recommend they invest in index funds..."

While I am an advocate of indexed investing, I do believe that some fund managers can generate excellent performance. Index tracking also has its own problems - would you buy a European Government Bond index now? In my view, a highly diversified portfolio of indices will do the job over the long term. If you have a large portfolio of assets, you might consider adding a low cost actively managed investment that aims to limit exposure to excessively priced shares. However, if you are unsure of what to do, stick with the index; even Warren Buffett thinks it's a good idea.