NJMoneyHelp.com
smart advice. every day.

April 4, 2016

Choosing a Single Mutual Fund

Q. If I can only be in one mutual fund, what should it be? I'm just starting out investing. — Starting out

A. Tough decision.

Mutual funds are a great way to make a first investment because they offer you the opportunity to own a variety of stocks or bonds with one purchase.

"Trying to pick one stock or one bond would be a much riskier way to invest your money and far less likely to be as successful a strategy as the fund would be," said **Claudia Mott, a certified financial planner with Epona Financial Solutions in Basking Ridge**.

That's because of diversification. Because a mutual fund is comprised of many individual stocks or bonds, the impact of one holding's performance on the overall portfolio is minimized, Mott said.

Before you get started, there are a few mutual fund characteristics you want to understand before making a decision about purchasing a mutual fund, Mott said.

Fees: Load funds charge a fee when the fund is purchased, which means you lose a piece of your investment right from the start. No-load funds have no initial purchase charges. Expense ratios are the cost to run the fund and are embedded in the price of the mutual fund, Mott said.

Management: Actively managed funds have an individual or a team making decisions on which investments will be bought and sold for the fund, she said. As a result, the expense ratios tend to be higher than those of index funds. An index fund is portfolio of investments designed to track a market index or segment. Well-known indexes such as the S&P 500 and small-cap Russell 2000 are examples, she said.

Style: Most mutual funds are designed to provide investors with exposure to a certain part of the capital markets. "It's important to know whether the fund you are considering invests in stocks or bonds, a particular size or maturity, has a focus on an industry or investing style," Mott said.

This information is readily available on the websites of the mutual fund companies.

With almost 8,000 mutual funds registered in the U.S., you have no shortage of options for your first investment, Mott said, suggesting you may want to consider a fund that is going to give you a chance to have a diversified portfolio right from the start.

One option is a so-called life cycle fund, also called a target date fund, which is designed to include a number of different types of mutual funds into a portfolio that has an allocation which is targeted toward the investor's age or risk profile, she said.

"These funds are often used in retirement accounts such as IRAs, but can be purchased in taxable accounts as well," she said. "There are also balanced funds that are usually comprised equally of stock and bond holdings and can provide diversification with one investment."

Another alternative would be to purchase a fund that invests in a broad segment of the U.S. stock market to establish a core position in your portfolio, she said. But in order to round out your portfolio, you'll need to add other types of funds down the road to ensure that you are diversified.

If you are going to purchase your fund in a taxable investment account — not an IRA or other retirement account — be aware that most mutual funds generate taxable income in the form of dividends and interest which will need to be reported on your tax return, Mott said. The fund may also have to take capital gains that will be passed on to you as a shareholder as well.

Email your questions to ask@njmoneyhelp.com