Tips & Hips, an Alternative to Mutual Funds

For many people, investing in equities poses some real problems. First, how do they know what companies to buy, and second, with their limited resources, how can they sufficiently diversify. This is where mutual funds came in. They provided an opportunity for the small investor to get a well-diversified professionally managed portfolio. This has been a good answer for many people, however, there is still a question of quality management.

Years ago, there were not that many funds to choose from, the managers were usually very experienced and not under excessive pressure to perform in the short run. Now, in Canada there are over 1,500 mutual funds, invested in endless types of investments, and current results are constantly scrutinized. You would think that this is good, but we are not so sure.

Unfortunately, this scrutiny is lead by the press, who are looking for stories, and as far as we can tell, are rarely qualified. Consequently, most papers publish things like the top ten and bottom ten producers for one year. We are sure that this gets a lot of attention, but truly, it is probably the most useless piece of information that you could ask for, especially when it includes all kinds of funds. If they have to publish this type of information, you would think that they would at least stick to ten year returns and segregate them by type of fund. But now we are becoming sidetracked.

The point is that all this scrutiny creates great pressure on managers to produce superior short-term results, even if it means sacrificing long-term results. So what should be a positive influence, may not really be a good thing. This can leave the investor in a difficult spot. If they want to invest in quality stocks, and have sufficient diversity, they either need to find a fund that is managed this way, despite the pressures, or have the resources to do it themselves. Of course many of our past issues have discussed ways to weed out these managers, but there is also another alternative, and it is a fairly low cost one, actually, over the long term, significantly lower in cost than mutual funds.

The Toronto Stock Exchange offers two very good alternatives. The first has been around for some time. The TSE 35 Index Participation Units or TIPS. You can buy TIPS through your stock broker in 100 board lots just like any other stock. But what you have bought is participation in a portfolio of shares weighted according to the TSE 35 index. You will receive dividends, if you own enough you can vote the shares like any other shareholder, and if you wish take possession of the underlying shares. The TSE 35 is adjusted annually to reflect the top shares on the Toronto Stock Exchange, so you are fairly assured that you are holding quality. There is no worry about what a manager is doing behind the scenes and best of all, no management fees. Your only costs are the broker fees to purchase and sell the units. While this is a good option, there has always been a concern that by sticking to thirty-five top companies, growth opportunities may be restricted.

Enter the TSE 100 Participation Units or Hips. Hips are relatively new and are very similar to TIPS, except that they hold stocks of one hundred different companies. This still leaves a high quality group of shares, but by being based on one hundred shares instead of thirty-five, there are some more aggressive companies included, leaving more opportunity for growth.

So, if you are concerned about mutual fund management, or are looking for another alternative to round out your Canadian equities, consider TIPS for a very conservative option or HIPS for a little more aggressive one. If you are looking for an American or International alternative, talk to your broker about similar foreign investments that are based on indexes like the Standard & Poors 500.

Some Information on the TSE 35 & 100 Indexes as of Dec. 31, 1997

Index	1 Yr. ROI	3 Yr. ROI	5 Yr. ROI	10 Yr ROI	3 Yr St.Dev
TSE 300 Total Return	15.0	19.1	17.5	11.0	3.6
TSE 100 Total Return	15.0	19.2	17.4	11.1	3.6
TSE 35 Total Return	16.4	20.2	17.9	11.3	3.6

It is interesting to note that while the standard deviations were all identical, the TSE 35, the most conservative did have a slightly higher return in every category. This only goes to show the value of quality.

Our review of the stocks in both TIPS and HIPs showed the following approximate weighings by sector.

Approximate percentage of shares by category

Index	Multi Sector	Financial Sector	Utility Sector	Consumer Sector	Resource Sector	Manufacturing Sector
HIPS		14 %	9 %	18 %	31 %	28 %
TIPS	3 %	17 %	12 %	17 %	37 %	14 %

The information on the above tables comes from sources that we believe to be accurate, however, it is not guaranteed.
