interactive investor

25 March 2022
By Faith Glasgow

ISA tips: funds and trusts investors can buy and forget about

A hands-off approach can work well for many types of investors. Faith Glasgow explains why and shares some fund and trust tips.

Stock markets can be scary places during times of global uncertainty and anxiety, such as at present. Active stock traders love the opportunities to exploit short-term pricing anomalies, while brave value investors will also be selectively bargain-hunting. But for many fund investors focusing on their pensions and ISA prospects, such periods of volatility can be very worrying.

It is at these times when a 'buy and forget' discipline really comes into its own. Selecting funds, investment trusts or ETFs for their long-term reliability and potential, and then simply not touching them for many years, regardless of market movements, means that you sidestep the temptation to panic and sell when volatility hits.

But buying and forgetting does mean cultivating a long-term perspective and concentrating on the wood rather than the trees. As Lee Wild, head of equity strategy at interactive investor, observes: "Stock prices have recovered from every war, bar none – the Second World War, Korea, the Gulf War, Afghanistan, Iraq, all of them. Only the time element changes."

The same applies in the case of other massive social and economic events such as the financial crisis. Wild adds: "It's worth remembering that the FTSE 100 traded as low as 3,460 on 9 March 2009. Even after the recent crash, it has more than doubled in value. Include dividends and the total return is over 200%."

Hands-off approach can work for core holdings

More generally, a long-term, hands-off approach can work well for many types of investors. It is a good starting point for younger investors, who may be short of spare hours now but have time on their side. It's also a sensible route for those interested in higher-risk parts of the market, where volatility is inevitable in the shorter term, but long-term rewards are likely to be great.

But buy and forget can work well for core holdings too. As a broad strategy, says Nick Wood, head of fund research at Quilter Cheviot: "It means investors are more resistant to all sorts of behavioural biases, not least the inclination to sell the weakest-performing funds and buy those doing better, which rarely ends well."

However, Rory McPherson, head of investment strategy at Punter Southall, explains that investors following a buy and forget strategy need to bear a few points in mind.

First, they should adopt at least a 10-year view of their investment, and he suggests opting for accumulation rather than income share classes so that dividends received are reinvested and growth is compounded. It also makes sense during this time "to try and remember to add to your holding on the dips, as opposed to panicking (and selling) during times of uncertainty".

Picking the right type of fund manager is key too, adds McPherson. "I'd encourage investors to find a manager who follows (and sticks to) a robust process that brings consistency to the returns pattern, as opposed to finding a ‘star' manager whose performance is much harder to predict and will require more ruthless monitoring, and whose star might fall as quickly as it rose.”

In addition, it is worth weighing up which vehicle might be best suited to this approach. “It may be a good idea to consider investing in investment trusts over open-ended funds, in that you have the comfort of the oversight of the board to work in the best interests of shareholders,” suggests Wood.

Index funds and ETFs: an easy way to buy and forget

One question in this context is whether it makes sense to opt for low-cost passive funds or ETFs that simply mirror the constituents of an index and follow its fortunes, rather than paying for more expensive active funds shaped by the stock picking and macro decisions of a fund manager.

With passive strategies there’s little monitoring to do beyond checking that it still meets your needs, because no fallible human fund management team is involved.

Rob Burdett, co-head of multi-manager solutions at BMO Global Asset Management, agrees that “if you are not interested in investment and/or don't want to pay for advice, passives are a great way to gain exposure to stock markets on a buy and forget basis”. However, he adds, the evidence indicates that over the very long term, active management clearly pays off. BMO’s research suggests that “the best active fund managers have delivered as much as five times the average passive fund over 20 years”.

Not only do good active managers have the drive and facility to outperform their benchmark, but they can also take action to reduce losses in a falling market. In contrast, passive funds are specifically designed to follow the index and so there is nowhere to hide.

What funds might you consider for a ‘buy and forget’ portfolio?

New investors looking for an easy, hassle-free solution might favour multi-asset funds such as those run by BMO. Dzmitry Lipski, head of fund research at interactive investor, picks out the BMO Sustainable Universal MAP Growth fund, “a one-stop, hybrid solution that incorporates actively managed multi-asset and sustainable investing with a focus on low cost”. The fund forms part of interactive investor’s Quick-start Funds range, which is aimed at beginner investors.

BMO’s Burdett makes the point, however, that “a pure equity fund will almost always have provided better returns for those with a longer perspective of seven years-plus”.

Possible ‘core’ pure equity choices could include Wood’s suggestion of the dividend stalwart City of London Ord CTY (up) 0.49%, a member of interactive investor’s Super 60. Wood points out that the investment trust operates "a very stable investment process that the manager has not deviated from over many years. It currently offers a yield of around 5% and gives investors exposure to the UK income market, which is arguably still fairly undervalued.” As mentioned above, those who don’t need the income can have it automatically reinvested.

As an open-ended fund alternative, McPherson likes the Artemis Income fund, which he says “follows a very clearly defined process that has made for consistency in performance even though elements of the team may change over time”.

More esoteric equity options for buying and forgetting include Lipski’s other choice, Montanaro Better World. This fund invests in small and mid-cap companies aiming to help solve some of the world’s major challenges by supporting the United Nations Sustainable Development Goals. Managers Charles Montanaro and Mark Rogers are highly respected small-cap specialists.

Other funds to consider are an Asia or emerging market fund to tap into favourable demographics, which include growing middle classes. Options in interactive investor's Super 60 list include Fidelity Asia, Guinness Asian Equity Income, JPM Emerging Markets and Mobius Investment Trust Ord MMIT (down) 0.69%.

Global listed infrastructure funds are another option, as often these assets – mobile phone towers, airports, toll roads – are inflation-proofed and structurally essential. McPherson suggests Clearbridge Legg Mason RARE Global Listed Infrastructure fund.

Multi-asset choices with a more focused capital preservation mandate could work well for investors reorganising their retirement portfolios and keen to sleep relatively easy at night.

Options include Troy Trojan or its closed-ended sibling Personal Assets Ord PNL (up)0.47% trust. Another wealth preservation option is Capital Gearing Ord CGT (down) 0.10%. The trust is another member of interactive investor's Super 60.

A similar multi-asset alternative is RIT Capital Partners Ord RCP (up) 0.75% investment trust, selected by Wood, which aims to outperform global equities and stay 3% ahead of inflation. "The mix of assets means it is more likely to protect capital in difficult markets, although it does not quite keep up in strongly rising markets," says Wood.

If you do want a cheap passive equity option, McPherson says Legal & General International Index "provides decent and low-cost exposure to a broad basket of global stocks".

Last but not least: the term 'buy and forget' is actually slightly misleading, as it would be a mistake to ignore any investment altogether for decades.

This shouldn't mean fretting over short-term relative underperformance, but could involve ensuring that the fund still does what you need it to do and its mandate hasn't changed.

Burdett adds: "Over the long run, the manager is likely to be replaced, so you will need to check they are still the same, equivalent or better. Equities have proved to be one of the best investments for over 100 years but keep an eye on the fees and volatility of the fund.