

The Worst Mutual Fund in the World

A staggering waste of investor money comes from an unusual group of suspects.

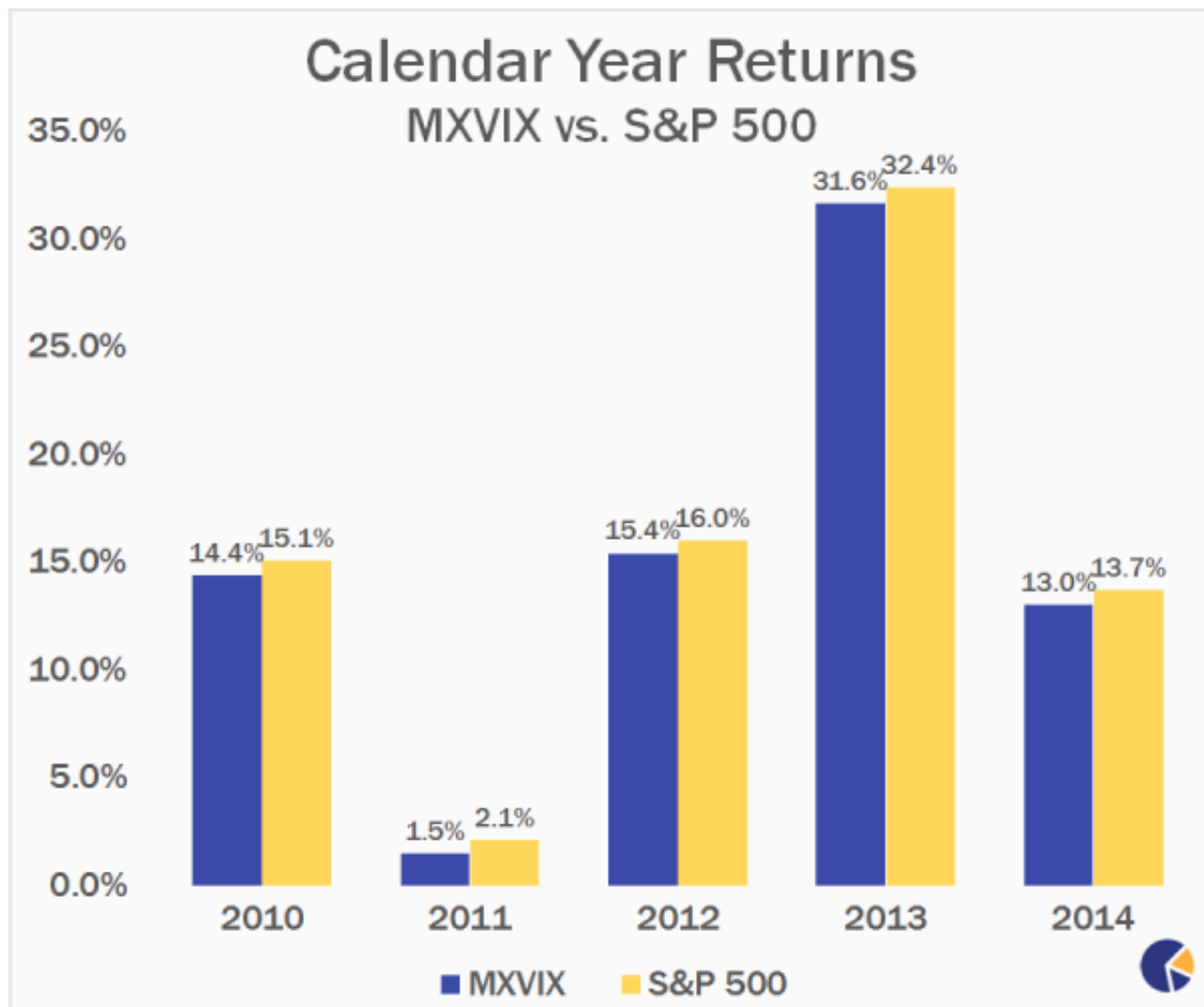
Based on the mountains of evidence illustrating the futility of active management, I am generally skeptical of non-indexed investment products. There is no shortage of targets for derision among the thousands of mutual funds; countless products charge sky-high fees in exchange for disappointing, benchmark-lagging results.

After reviewing hundreds of worthy candidates, I think I've found the Worst Mutual Fund in the World.

Here's the plot twist: the Worst Mutual Fund in the World is not an absurdly expensive fund run by a manager pursuing some exotic strategy. It's actually an index fund that seeks to replicate one of the most widely-followed benchmarks in the world. Wondering how such a product could be the target of such scorn from a fan of indexing? Easy: charge investors 60 basis points to track the S&P 500.

Yes, there is a mutual fund that charges an annual 0.60 percent expense ratio to replicate the S&P 500. The Great-West S&P 500 Index Fund (MXVIX) is a pretty straightforward fund. It holds the stocks of the S&P 500, seeking to replicate the benchmark. And it does so quite efficiently — before fees are considered at least. Like other well run index funds, MXVIX lags behind its related benchmark every year by an amount equal to the expense ratio.





Data Source: [Great West](#)

Most pricey mutual funds offer the possibility, however unlikely, of consistently delivering excess returns to investors. MXVIX, on the other hand, offers a guarantee of the opposite: it will underperform other products that implement an identical strategy every single year.

Monopoly in Action

MXVIX is hardly a unique product. There are more than a dozen mutual funds with an identical mandate to replicate the S&P 500. Some of them have expense ratios of less than 10 basis points. With fees as the only difference, MXVIX will underperform these comparable products 100 percent of the time. And thus it would be expected to attract very little in assets.

Here's the second twist: MXVIX has \$2.2 billion in assets. Yes, with a "b."


So what in the name of [Jack Bogle](#) is going on here? What rational investor would choose to pay 60 basis points annually when there are otherwise identical products available at less than one-fifth of the price?

The explanation is that most of those who end up investing in MXVIX have no choice. It's one of the handful of funds on the menus of 401(k) and 457(b) plans offered through their employers; if they want to take advantage of a tax-advantaged retirement plan and want exposure to the S&P 500, there's one game in town. And it's not cheap.

There are a number of online forums where investors [seek advice](#) about an optimal 401(k) strategy, and in many cases their options will make a [Boglehead cringe](#). Consider one such plan that offers participants a choice of 13 funds:

Name	Ticker	Expense Ratio
Great-West Lifetime 2015 Fund II T1	MXLWX	0.96%
Great-West Lifetime 2025 Fund II T1	MXDLX	1.02%
Great-West Lifetime 2035 Fund II T1	MXJLX	1.07%
Great-West Lifetime 2045 Fund II T1	MXPLX	1.09%
Great-West Lifetime 2055 Fund II T1	MXVLX	1.10%
American Funds EuroPacific Gr R3	RERCX	1.14%
Virtus Emerging Markets Opportunities A	HEMZ	1.57%
Great-West S&P SmallCap 600 Index Fund I	MXISX	0.60%
Great-West S&P Mid Cap 400 Index Fund I	MXMDX	0.60%
Great-West S&P 500 Index Fund I	MXVIX	0.60%
Invesco Comstock A	ACSTX	0.82%
MFS Growth R3	MFEHX	1.01%
Metropolitan West Total Return Bond	MWTNX	0.86%

As of January 2015.



Data Source: [Reddit](#)

The choices here are infuriating for anyone who understands how expense ratios translate into dollars over an extended period of time.

Retirement plans such as this one are the explanation for the \$2.2 billion in MXVIX. It's the mutual fund equivalent of a \$9.50 Bud Light at a baseball game. The bar across the street is selling the exact same product for \$2.50, but is (at least temporarily) off limits.

Great-West is the beer man at Wrigley Field, selling a widely available product at a wildly inflated price.

With no other suppliers of either Old Style or the S&P 500 to be found, the crowds line up to fork over their money. Most of them know the price is absurd, but it's the only game in town.

\$114,000 Price Tag

Frustration with a 60 basis point expense ratio may seem extreme. Surely the impact of an extra half a percentage point in fees is nominal, right?

Yes and no.

The fees on a \$6,000 investment in MXVIX made in the first year of employment would total about \$21. If a similar S&P 500 fund with a 10 basis point expense ratio were used instead, the fees would be about \$3. That \$18 isn't going to make or break your retirement.

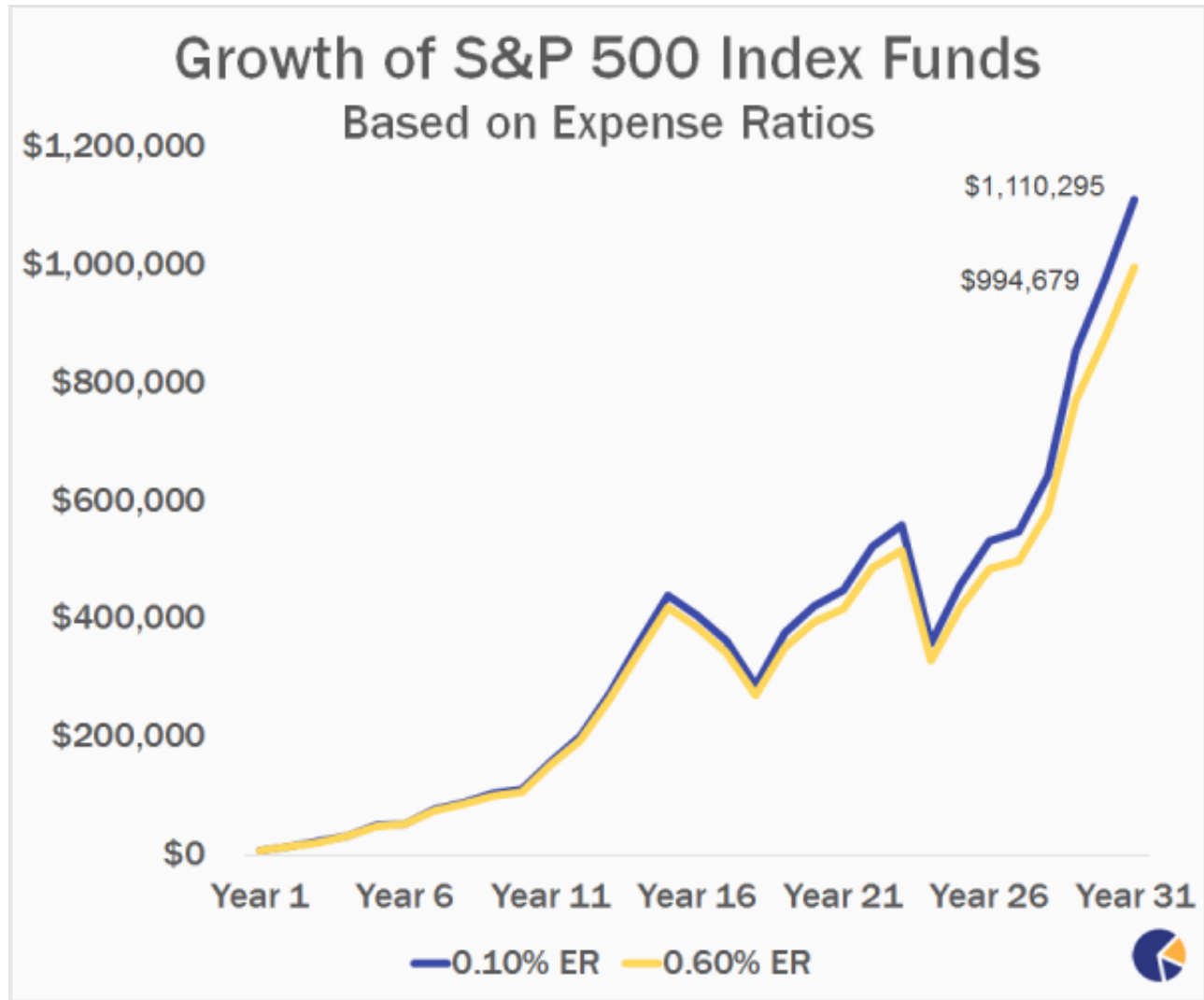
You'd probably feel quite differently about a difference of \$114,000 though.

Assume a scenario in which:

1. An employee contributes the maximum \$18,000 to a 401(k) each year, and receives a \$2,000 employer match for a total of \$20,000;
2. The employee allocates 30 percent of contributions to an S&P 500 fund; and
3. The S&P 500 delivers the same returns it did each year between 1985 and 2014.

At the end of 30 years, the value of the S&P 500 fund will vary depending on the expenses charged. MXVIX would be worth about \$995,000. That represents a significant growth of the \$186,000 in contributions that would have been made over the three decades, so it would be hard to be too disappointed in the outcome. But you should be.

A similar index fund that charges a more reasonable 10 basis points annually would be worth about \$1,110,000. In other words, the lack of competitive pricing costs plan participants about \$114,000 over the course of 30 years.



Assumes the annual returns delivered by the S&P 500 between 1985 and 2014.

Being gouged for a cold beer at the ball park is tolerable. Losing out on \$114,000 in your retirement account isn't.


“Last Bastion of Gluttony”

Rick Ferri has said that “the last bastion of gluttony in the investment industry is stubbornly high financial advisor fees.” I'd argue that the exorbitant expense ratios on funds designed to have a monopoly on 401(k) contributions belong on that list as well.

Financial literacy has increased significantly in recent years, and the trend toward fee-only advisors and low-cost funds is certainly encouraging. But in many 401(k) plans and elsewhere, absurd expense ratios remain the norm. And in some cases, the trend is going the other way; Great-West recently launched a new share class of its S&P 500 Index Fund — with an 85 basis point expense ratio.

If you think I've been unfair to MXVIX, you're right. It's not the Worst Mutual Fund in the World, though it's certainly an awful product. But it's actually quite a bit **cheaper** than several other S&P 500 index funds that insurance companies and other firms offer to 401(k) participants.

Fund	Ticker	Expense Ratio	Cost [a]
State Farm S&P 500 Index Fund	SNPBX	1.44%	\$281,666
Principal Large Cap S&P 500 Index Fund	PLPIX	1.03%	\$204,713
MainStay S&P 500 Index Fund	MYSXP	0.78%	\$154,013
Nationwide S&P 500 Index Fund	GRMCX	1.20%	\$237,524
PNC S&P 500 Index Fund	PPIX	1.20%	\$237,524
Invesco S&P 500 Index B	SPIX	1.37%	\$269,048

[a] Reflects difference in value after 30 years, assuming 1985 to 2014 returns and \$6,000 annual contributions, relative to 10 basis point S&P 500 Index Fund. 

Fund Reference editor in chief Andy Hagans [has suggested](#) that investors should get in the habit of a portfolio “spring cleaning” where they review their allocations and trim unnecessary expenses. Unfortunately, there isn't always a better alternative.

The tax advantages — and hopefully the employer matching — of 401(k) plans make them an important part of a retirement plan. But maximizing such advantages often requires consenting to highway robbery at the hands of monopolistic fund.

If your 401(k) options are limited to gluttonous funds, your options are limited. But you're not completely powerless. If you ever leave the company, grab the paperwork needed to [roll over into a more flexible IRA](#) on your way out the door. In the meantime, send this article to the administrator of your company's plan. Let them know that the plan they selected is costing you dearly, and request the addition of some low-cost funds to the menu. Who knows? Enough frustration may translate into action.

The days of 401(k) gluttony are numbered, but there is a strong incentive to squeeze out every last penny. Let's make sure more of those hard-earned pennies fund **your** retirement and not your fund manager's.

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