The $25 billion annual mutual fund rip-off

Defined benefit pension plans achieved much higher returns than mutual funds, according to a recent comprehensive study. This means that workers need to invest far less in defined benefit pensions plans than in mutual funds to achieve a decent retirement income.

During the past year, our media has printed many stories about shortfalls in defined benefit pension funds. But in reality, it is those without workplace pensions, who have suffered from continual shortfalls and crises from their mutual fund investments.

A comprehensive study by Canadian pension fund expert Keith Ambachsheer has found that defined benefit pension plans in Canada achieved annual average returns at least 3.8% higher than mutual funds with comparable investments.

Defined benefit pension funds outperformed the market by 1.23% per year, while mutual funds had average returns that were 2.6% below the market during the 1996 to 2004 period. Returns for most mutual investors were even less than this, as a result of sales fees and consistently poor selection of mutual funds by misinformed investors: buying high and selling low.

This means that those with savings in mutual funds lost a total of about $25 billion a year from the higher management fees and lower returns compared to workplace pension funds. Higher management fees are responsible for about $15 billion of this.

If these trends continue, those depending on private mutual funds will have retirement pensions that are about 40% lower than defined benefit pensions plans for the same amount invested. In the example used by the study of a $45,000 annual pension, this means $20,000 less per year for retirees.

Where has this money gone?

Most of the difference in returns is because of much higher management fees charged by the mutual fund industry, which have generated massive profits for the banks, sky-high salaries in the investment industry and expensive ad campaigns. But even before these fees, mutual funds achieved 1% lower returns than pension fund equity investments.

This hasn't just been a problem in Canada. The study shows that defined benefit plans in the United States achieved average annual returns 2.66% higher than comparable mutual funds.

These results prove in very concrete terms just how much better workplace pension plans -- and especially defined benefit plans -- are for providing decent security in retirement. Unfortunately, less than 30% of Canadian workers belong to defined benefit pension plans.

CUPE's Multi-Sectoral Pension Plan (MSPP) provides an excellent opportunity for workers in smaller bargaining units to join a decent pension plan with over 4,400 members.

Keith Ambachtsheer and Rob Bauer, "Losing Ground", Canadian Investment Review, Spring 2007.
<http://www.investmentreview.com/archives/2007/spring/spring2007losing%20ground.html>

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