
Trackers follow the market, so you don't have to worry about which fund manager's strategy is best

On the right track

Tracker funds are a low-cost way to invest in the stock market – we help you to decide whether they are right for you

If you're looking for a low-fuss, low-cost way into the stock market, tracker funds could be for you. Unlike many other financial products, tracker funds do exactly what they say on the tin. Come rain or shine, they try to track the performance of the stock market, whether it goes up or down.

The advantage of this is that if you are watching the news and see that the stock market has gone up, you know that your investment has also gone up. This means you don't have to worry about whether your fund manager has had the insight to invest in the right companies' shares.

In this report we explain what trackers are and how they work, and give you information about the different markets you can invest in. We will also help you decide whether tracker funds are the right investment for you. Trackers aren't for everyone, as there are always risks involved when dealing with the stock market, but if you are in a position to invest, the Best Buys in our table of UK tracker funds, overleaf, should set you on the right track.

We answer your queries

Q What is a tracker fund and how does it differ from other funds?

A A tracker attempts to mimic the performance of the stock market by trying to track an index, such as the FTSE 100 which consists of the UK's largest 100 companies – see 'About indices', p31, for more details about how an index works. By contrast, an actively managed fund has a fund manager who picks shares they think will beat the market.

Q Why track the market instead of trying to beat it?

A Over the past five years, just over half of the actively managed funds in the UK All Companies Sector outperformed the average tracker – bad news for you if your fund happens to be in the wrong half. With trackers, you know your investment will roughly match the performance of the index, minus any charges. This avoids the problem of working out which fund manager's strategy is most likely to succeed.

Q Are there different types of tracker fund available?

A The majority of funds track UK and overseas stock markets, others track the performance of government or corporate bonds. The widest choice of funds available is among those that track the UK stock market. Most of these track either the FTSE 100 index or the FTSE All-Share index, which represent the broader London stock market.

Q How do the charges compare with an actively managed fund?

A Trackers usually have lower charges because they are less complex to manage and do not need as much research, as they're not trying to beat the market. In fact, many trackers rely heavily on computers to decide what stocks the fund should hold and when to buy and sell.

Most trackers don't have an initial charge and their annual charge for running the fund is less than 1 per cent. For a comparison of total tracker charges, see the table on p31.

Most trackers don't have an initial charge

By contrast, an actively managed fund's initial charge is usually around 5 per cent of your investment and its annual charge is about 1.5 per cent. So for an investment with these charges to break even, let alone make a profit, it must increase by at least 6.5 per cent in the first year.

Q Are there any risks involved with investing in trackers?

A Trackers aren't a risk-free way to invest in shares. By investing in a tracker, you're tied to the ups and downs of the stock market and your chances of making a profit or a loss will reflect that.

You should invest in a shares-based tracker only if you're prepared to invest for at least five years and you can cope with the possibility that you may lose money. If you can't face this, don't invest.

But if you're comfortable with the risks and are content to follow, rather than try to beat, the market, trackers are a straightforward and low-cost way to get into the stock market. It's best to pick a tracker with low charges – our research shows this is more important than how well it tracks as most funds have a low tracking error.

Q **What is the best way to invest in a tracker fund?**

A Most trackers offer the chance to invest lump sums and make monthly contributions. If you are a novice investor, it's best to go through a financial adviser. Not only will they help you decide which tracker to invest in, but you also have access to redress through the Financial Ombudsman Service if the advice you receive is unsuitable for your needs. You may have to pay your adviser a fee; ask beforehand. We recommend you see an independent adviser with investment expertise – IFA Promotion (see 'Contacts', below) will help you find one.

Alternatively, if you are comfortable investing on your own, you can buy trackers directly from either the provider or a fund supermarket – see 'Contacts' for details of the providers in our table. However, if you buy without taking financial advice, you have no redress through the Financial Ombudsman Service if the tracker's not suitable. So buy directly only if you are confident that you know what you are doing.

It's best to pick a tracker with low charges

TRACKERS IN PRACTICE

Geof Nuttall *75, retired*

Geof Nuttall has been investing in trackers for many years and has tracker funds invested in all of the major world stock markets. He even has trackers that invest specifically in technology and healthcare firms.

Geof says: 'My reasons for using trackers are simple: low charges and being content that I receive an average performance. I dislike paying for someone else to gamble with my money, especially when so few of the active managers actually beat the markets.'

Over the past couple of years, Geof has been increasingly using ETFs (see 'Flexible funds', p31), again investing his money across major world stock markets. Geof told us: 'These have effectively taken over from conventional trackers for me because they are much cheaper to buy and run.'

Geof has his tracker fund strategy sorted and is now looking forward to many years of reassuringly average returns.

Contacts

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Axa UK
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Direct Line
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Engage Investment
0800 028 6248
www.engagemutal.com

Fidelity
0800 414161
www.fidelity.co.uk/tracker

Gartmore UK
020 7782 7000
www.gartmore.com

Halifax UK
0845 600 0845
www.halifax.co.uk/investments

HSBC
0800 181890
www.hsbcinvestments.co.uk

IFA Promotion Ltd
0800 085 3250
www.unbiased.co.uk

Insight Investment
0845 777 2233
www.insightinvestment.com

Legal & General UK
0800 092 0092
www.legalandgeneral.co.uk

Liontrust
020 7412 1766
www.liontrust.co.uk

M&G
0800 389 8600
www.mandg.co.uk

Marks & Spencer
0808 002 2222
www.marksandspencer.com

Nationwide
0845 930 2010
www.nationwide.co.uk/investments

Norwich UK
0845 302 2559
www.norwichunion.com

Prudential UK
0800 072 6159
www.pru.co.uk

Virgin UK
0845 610 2020
www.virginmoney.com

USING THE TABLE

We show details of tracker funds available through a unit trust or open-ended investment company in the UK All Companies Sector. Funds must have been available for five years to be included, have no initial charge and a minimum initial investment of £2,500 or less. We've included trackers that track the two main UK indices – the FTSE 100 and the FTSE All-Share. The best (in red) are those that have the lowest charges.

Minimum investment

Initial The minimum initial investment into the fund. **One-off** The minimum irregular, or one-off, payment accepted. **Regular** The minimum regular payment accepted – monthly, for example.

Tracking

Tracking error We compared the value of £1,000 invested in the tracker fund and the index it is tracking each month for a total of 60 months – charges are excluded from this analysis. Any difference between the fund's performance and the index it tracks is counted as a tracking error. We calculate an average monthly percentage tracking error for each fund. The lower the errors, the better the fund tracks the index.

Charge

Total expense ratio The total annual cost of running the fund, including the annual management charge, any set-up costs, and auditing and legal fees. This cost is charged as a percentage of your investment.

PHOTOGRAPHY CAMERA CREW, GETTY IMAGES, ALAMY

Flexible funds

Exchange-traded funds are a low-cost way to track shares, bonds and other markets around the world

Exchange-traded funds (ETFs) are investment funds that aim to track a specified index, such as shares or bonds. They work in a slightly different way from conventional tracker funds and are usually cheaper.

You invest in ETFs by buying shares in the fund, and ETFs are quoted on the stock market like shares and are bought and sold through stockbrokers. Unlike UK shares, you don't pay stamp duty on ETF purchases.

There is a huge range of indices available to track, including shares, bonds and commodities, such as gold. iShares (www.ishares.co.uk), run by Barclays Global Investors, is the best-known ETF provider. It offers a choice of 32 share indices and 13 bond indices.

The total cost (otherwise known as the total expense ratio – see 'Using the table, p30, for details) of investing in an ETF ranges from 0.2 per cent for many of the bond funds to 0.74 per cent for ETFs tracking Far Eastern and other emerging stock markets. The iShares FTSE 100 ETF, which tracks the 100 largest UK companies, costs 0.4 per cent a year.

There's extra risk if you buy ETFs that track overseas markets. This is because they are usually priced in either US dollars or euros, so any changes in exchange rates will affect your return.

TRACKER FUNDS	MIN INVESTMENT (£)			TRACKING	CHARGE
	INITIAL	ONE-OFF	REGULAR	TRACKING ERROR (%)	TOTAL EXPENSE RATIO (%)
FTSE ALL-SHARE TRACKERS					
FIDELITY MONEYBUILDER UK INDEX FUND	500	250	50	0.52	0.3
M&G INDEX TRACKER FUND	500	100	10	0.54	0.46
GARTMORE UK INDEX FUND	1,000	250	50	0.52	0.5
LEGAL & GENERAL UK ALL SHARE INDEX TRACKER TRUST	50	500	50	0.56	0.51
HSBC FTSE ALL SHARE INDEX	1,000	500	50	0.52	0.64
ALLIANZ RCM UK INDEX FUND A SHARE	500	500	50	0.52	0.67
NORWICH UK INDEX TRACKING SC 1	1,000[a]	250	50	0.10	0.94
AXA UK TRACKER	1,000	500	na	0.37	0.99
VIRGIN UK INDEX TRACKING TRUST	1	1	1	0.16	1
NATIONWIDE TRACKER FUND	20	20	20	0.52	1
INSIGHT INVESTMENT FOUNDATION GROWTH CAT FUND	500	500	50	0.55	1
HALIFAX UK FTSE ALL-SHARE INDEX TRACKER C	500	50	50	0.38	1.5
FTSE 100 TRACKERS					
LIONTRUST TOP 100 FUND	2,500	1,000	50[b]	0.52	0.4
PRUDENTIAL UK INDEX TRACKER TRUST	500	250	50	0.61	0.5
NORWICH BLUE CHIP TRACKING SC 1	1,000[a]	250	50	0.60	0.96
DIRECT LINE FTSE 100 TRACKER FUND (STANDARD CLASS)	1,000[a]	1,000[c]	30	0.45	1
GARTMORE UK TRACKER FUND	1,000	250	50	0.60	1
ENGAGE INVESTMENT GROWTH A	600[a]	500	30[d]	0.61	1.03
MARKS & SPENCER UK 100 COMPANIES FUND	100	25	25	1.08	1.03
HSBC FTSE 100 INDEX	1,000	500	50	0.59	1.4

a Minimum £500 within an Isa **b** Regular investment allowed only within an Isa **c** Minimum of £200 within an Isa **d** Minimum of £20 within an Isa

All figures correct as at 14 March 2007

Checklist

Am I in a position to invest?

Consider trackers or other share-based investments only once the rest of your finances are sorted. That means:

- **No debts** Being debt-free (apart from a mortgage).
- **Rainy day funds** Having emergency savings of three to six months' spending so you could survive temporarily if you lost your livelihood.
- **Planning ahead** Making sure you get life insurance if you have dependants.
- **Income protection** Being protected, either through your work or an income-protection policy, in case you couldn't work because of illness or accident.
- **Pension** Being a member of your employer's pension scheme or having your own pension. If you have your own pension, you may be able to invest it in trackers.

If trackers are for you

- **Isas** Most tracker funds are available as an Isa – see 'A brand new Isa age', *Which?*, March 2007, p20, for more information about Isas.
- **Risky business** Remember that trackers are not risk free. The stock market can go down as well as up.

About indices

An index is a number that shows changes in the value of stocks and shares. There is at least one index for each stock market. For example, the FTSE 100 is an index that represents the biggest 100 UK companies, and the FTSE All-Share represents the London market. Changes in the shares' value are averaged to create the index. This gives a picture of how the overall market has changed.