A Sensible Approach on When to Redeem Your Funds

There is no lack of advice on why and when we should buy unit trusts. However, when it comes to selling or redeeming them, getting the right timing and the reasons for doing so may prove to be a difficult task.

Unit trusts are excellent vehicles for individuals and corporate financial planners due to their affordability, liquidity and flexibility. For medium- to long-term investing, unit trusts are an undeniably attractive option. Chosen with care and supported by qualified advice, unit trusts can earn you healthy returns at acceptable levels of risk. However, just like any other investments, we should follow certain sensible guidelines on when to hold and when to let go.

The most common advice is to start investing early, and to give your investment enough time to reap its returns. But what if a volatile market causes you to consider switching your equity funds into bond and money market funds? The decision you make will depend on the state of your investment portfolio, financial goals and risk tolerance. Nevertheless, it is important to first establish sound and sensible reasons for doing so. Here are some issues one should consider when deciding when to redeem a unit trust investment.

A Fund's Performance

The most common reason for redeeming a unit trust fund is when the fund has registered a loss for investors. However, many investors make the mistake of redeeming on the basis of a fund's poor performance over a short-term period. Volatility exists in the market and judging a fund's performance over short-term periods is a mistake as unit trust investors are required to take a medium- to long-term view in order to reap the full potential of their investments. If your fund's performance has been affected by adverse market conditions, you should remain focused on the long-term prospects of your investment and avoid the temptation to panic.

"Unit trust investors should remain focused on achieving their investment goals over a medium to long term period of three to five years rather than worry about the daily, weekly or monthly movements of their investments," says a fund manager.

Deviations in Fund Style or Objectives

After having carefully done a detailed asset allocation plan, investors should choose a fund (or funds) that best matches their strategy, taking into consideration the return objectives, time horizon and risk tolerance. Making the right choice of funds is important because if the fund takes more risk than what you can tolerate, you may have to redeem the fund and buy a more suitable fund. In addition, if a fund deviates from its original investment objective or investment style, such changes can almost assuredly affect your asset allocation plan and require a relook. A fund that significantly changes its investment objectives could cause its performance to deviate from your desired objectives and risk profile. Thus, it is vital to remember the original reasons for buying a fund.

A change in fund managers can also be a cause for a change in investment style. However, it does not require an automatic sell response. On the contrary, what is more pertinent is to ensure the new manager has a good track record in managing funds with similar objectives and will maintain a similar management style. A fund managed by a stable and reputable management team will tend to adhere to its objectives and investment style.

In case of emergency

Because unit trusts are easily liquidated, unitholders may redeem all or part of their units on any business day and the unit trust manager will purchase them. This means that should you need cash, you can easily sell the investment. Most unit trusts will allow you to redeem your investments on any given business day.

However, it is important to look for alternatives as redeeming could hurt you in the long run – you lose the benefits of Ringgit-cost averaging and compounding interest. For those who really need to liquidate their investments, consider the "average-cost method" which entails selling in stages. Investors moving out of a particular asset class can then slowly move into cash to prepare ahead of a financial commitment such as education expenses.

The bottom-line is that if you have been contemplating about redeeming your fund, do consider the reasons and ensure that they are based on sound considerations. Rebalancing your portfolio based on your changing needs or situation should of course, be done on a regular basis of at least once a year. If you plan to redeem just to switch to another fund or because you are nervous about market conditions, take control over your impulses and remember the principles of an appropriate asset allocation strategy. A wisely selected fund that is well-diversified should help you achieve your long-term investment goals.