Why Mutual Fund?

ADVANTAGES OF MUTUAL FUNDS

- A professional portfolio manager, who searches for the most attractive assets and securities for the fund, manages a mutual fund. The managers do all the footwork - they uncover opportunities and research them to make sure the investment is appropriate for the needs of the fund. The fund's stated goal, or investment objective also influences the choice of securities.

- Another benefit of mutual funds is *liquidity;* the ability to move money in and out of the investment. Unlike fixed deposits or CDs where money is tied up for a period of time, mutual funds are designed so that access to investment money is easy. The investor can move money from one mutual fund to another, make withdrawals, or set up regular investment plans that help build up assets over the long term.

- Mutual Funds substantially lower the investment risk of small investors through diversification in which funds are spread out into various sectors, companies, securities as well as entirely different markets. It is always the objective of a fund manager to maximize a funds return for a given level of risk through a tolerable risk-return tradeoff.

- Mutual Funds mobilize the savings of small investors and channel them into lucrative investment opportunities. As a result, mutual funds add liquidity to the market. Moreover, given that the funds are long term investment vehicles, they reduce market volatility by offering support to scrip prices.

- Mutual Funds provide the small investor access to the whole market that, at an individual level, would be difficult if not impossible to achieve.

- Because funds are professionally managed, investors are relieved from the emotional strain associated with the day to day management of the fund. Moreover, the amount of analytical research and study that goes into selecting the best securities for a fund portfolio can prove to be overwhelming for the individual investor, and is best left to the experts.

- The investor saves a great deal in transaction costs given that s/he has access to a larger number of securities by purchasing a single share of a mutual fund.

- The investor can pick and choose a mutual fund to match his/her particular needs.

MUTUAL FUND OBJECTIVES

Mutual Funds are designed with specific investment objectives to fulfill the particular needs of the investor. There are different funds for different investors. By offering this sort of variety, mutual funds have been able to attract a broader client base. There are many categories of funds:

Income Funds invests in bonds and high yielding stocks such as utility companies and blue chip companies that offer high dividends. The objective of this type of fund is to maximize the current income of the investor while at the same time providing a secure investment.

Growth Funds investment focus is on growth stocks and newly incorporated companies with the potential of high capital appreciation, but lower dividend yields.

Balanced Funds focus is on a diversified investment both in stocks and bonds, however, the fund maintains a limit of how much to invest in each category.

Index Funds is composed of securities that make up a particular market index and consequently, the performance of the fund mirrors the performance of the index.

TYPE OF MUTUAL FUNDS

Mutual Funds can be classified into two basic categories:

Open-End Funds :

This type of fund can sell an unlimited amount of shares to the investors, using the proceeds to increase its investments and consequently the size of the fund. Likewise, the investors can also sell their shares back to the Investment Company at any time, and redeem their funds at the Net Asset Value (value of all assets held by the fund divided by the total number of shares outstanding) of the fund at a particular time.

Close-End Funds :

The number of shares that the fund can sell to the investors is restricted by the number of shares sold in the initial public offering of the mutual fund. The shares of a close-end mutual fund are traded like any other equity security in the open market, i.e. the price of the share is determined by demand and supply. Furthermore, the shares are listed on the stock exchange. Consequently, unlike the open-end fund, the redeemable value of these shares is not the NAV of the fund, but the price of the share as quoted on the exchange. Hence, it is not unusual to find close-end funds trading at a considerable premium or discount to their NAV.

However, Close-End Funds can have a predetermined life, after which it is redeemed, on disposal of assets, which is equitably distributed among the unit holders.

INCOME & GROWTH: WAYS TO GO

A mutual fund investment has the potential to earn in two basic ways. The first is income: a mutual fund passes along dividends and interest it receives from the securities it owns. One can choose to have these *distributions*, as they are called, withdrawn or reinvested and used to buy more shares of the fund.

The second way to earn is *growth*, also known as *capital appreciation*: as the value of the securities in a portfolio increases, a fund's share price increases, meaning that the value of the investment rises. If the investor sell shares at a higher price than s/he paid for them, a profit or *capital gain* is made and vice versa.

It is important to know in advance how much change in share price one can tolerate, so that s/he can choose a mutual fund that suits the individual comfort level. Some mutual funds are designed for little or no fluctuation in share price, while others are comparatively volatile.

VALUE & OWNERSHIP OF MUTUAL FUNDS

Mutual fund ownership comes in the form of shares. As a shareholder, one can own a certain number of fund shares, depending on how much money s/he has invested in the fund. The investors will receive their portion of the gains or losses the fund experiences over time.

Every mutual fund has a share price: the value of one share in the fund. With most funds the value is calculated daily, because the value of a fund's securities changes every day in response to the movements of the price of the assets, i.e. the stock, bond and money markets. The per share value is calculated by dividing the value of the securities in the fund by the number of shares in the fund.

CRITICAL FACTORS FOR MUTUAL FUNDS

As with any other financial institution, the reputation of the sponsors, along with the managing institution of the mutual fund i.e. the Asset Management Company, is the key factor in inspiring investor confidence to entrust their savings to the Investment Company.

A mutual fund will fail to succeed if it does not have the support of strong technical and fundamental research material. A professional research staff is necessary for quality stock picking to be able to pick out the gems from the array of stocks. Also the importance of sales and settlement cannot be over-emphasized as timely execution along with timely entry and exit points into the market would make all the difference in a fund's performance.