

# Mutual Fund Investing

Mutual funds are one of the most popular ways to invest. That's not too surprising given their flexibility and convenience. Experienced investors, as well as individuals who are just starting to invest, can use mutual funds to help achieve their investment goals.

## What Is a Mutual Fund?

A mutual fund is an investment company that pools the money from investors who buy shares of the fund. A professional investment advisor(s) manages the pooled money as a single account, investing in a variety of securities that reflect the fund's goals. A mutual fund may hold hundreds of different securities in its portfolio.

A mutual fund seeks to make money for investors by earning dividend or interest income on the securities in the fund's portfolio and by selling investments that have increased in price. Mutual funds distribute most of their income (net of expenses) to their shareholders in the form of periodic dividends. Distributions of net capital gains generally are made at the end of the year. Investors usually have a choice of reinvesting their dividends and distributions in additional fund shares or receiving a check (or other form of payment).

Mutual fund shares are bought and redeemed (sold back to the fund) at the fund's current "net asset value" (NAV) per share. The NAV reflects the value of the fund's assets minus its liabilities. A fund's NAV fluctuates almost daily as the values of its holdings change.

Some funds impose shareholder fees when shares are purchased or redeemed. In addition, funds have annual operating expenses and fees that lower investor returns. Investors can find information about these charges in a fund's prospectus.

## Why Invest in Mutual Funds?

Mutual funds provide investors with several advantages. These include:

**Diversification.** Investing in a mutual fund is generally less risky than investing in a single security (such as the stock of one company) because a mutual fund is already diversified. If one or more of a fund's investments lose value, others may gain value or hold steady, helping to cushion the losses. To provide additional diversification, individuals can invest in several types of funds. However,

diversification does not ensure a profit or protect against loss in a declining market.

**Professional management.** A variety of economic, political, and financial factors can influence the value of securities. Fund managers have access to resources that allow them to analyze relevant data and screen a universe of securities to identify those with the greatest potential.

**Liquidity.** Shares in mutual funds generally can be bought and redeemed every day the markets are open.

**Convenience.** Investing in a mutual fund is often only a phone call or a mouse click away. Many funds require only a small initial investment, and subsequent purchases often require a modest minimum investment also.

## Major Mutual Fund Categories

There are two broad categories of mutual funds — *passive* and *actively managed*. Passive funds, also called *index funds*, attempt to replicate the performance of a broad market — or a market segment — by buying the same securities that make up a market index, such as the Standard & Poor's 500 Index (an index of the stocks of 500 major corporations). With an actively managed fund, the fund's managers actively direct the portfolio in an attempt to outperform market benchmarks. Numerous types of funds are available within these broad categories.

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**Stock funds.** Within the stock fund category, there are funds composed solely of large-, mid-, or small-capitalization stocks. Capitalization is simply the total dollar value of a company's stock at any one point in time, as measured by the number of outstanding shares multiplied by the stock's price. Although different managers may use different dollar ranges to assess whether a stock is a large-, mid-, or small-cap stock, in general:

- Large-capitalization funds hold stocks of large, well-known companies. They offer the potential for long-term capital appreciation.
- Mid-capitalization funds hold stocks of medium-sized companies. Like large-capitalization funds, they offer the potential for long-term growth.
- Small-capitalization funds generally own shares in companies in the early stages of their growth, whose shares could rise (or fall) in value significantly.

Stock funds also may follow a growth or value strategy. Growth stocks are stocks of companies thought to be capable of higher than average earnings growth. Value stocks are considered to be "bargain priced," since they are priced lower than stocks of similar companies in the same industry. The premise behind value investing is that the stocks may realize their potential down the road, and investors will reap the profits.

Stock investing involves a high degree of risk. Stock prices fluctuate, and investors may lose money.

**Bond funds.** Some bond funds hold only U.S. government bonds, while others specialize in municipal securities or corporate bonds. Other funds hold a combination of government and corporate securities. Likewise, some bond funds hold only bonds with long maturities, others specialize in shorter term debt, and still others hold a combination of both.

During periods of stock market volatility, bonds may provide some stability, since they often increase in value when stock values fall. A portfolio that includes funds holding intermediate- or long-term bonds commonly has the potential to earn returns that are greater than the rate of inflation.

As with any investment, however, bond investors face various risks. For example, bond prices often fluctuate due to interest rate changes. Experienced bond fund managers understand these risks and take a variety of steps intended to manage them.

**Money market mutual funds.** These funds invest in what are widely considered to be low-risk, short-term investments, such as Treasury bills and certificates of deposit (CDs). Typically, money market funds try to maintain a stable \$1 per share value, although it is possible for investors to lose money. An investment in a money market mutual fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency.

Since the risk of losing money is low, the total return of a money market fund is typically relatively low. Returns may not keep pace with the annual inflation rate.

### Other Types of Funds

The mutual fund universe has many other variations within these main themes. For instance, balanced funds hold stocks and bonds in their portfolios to provide the potential for both growth and income. International funds hold shares in non-U.S. companies and/or bonds of foreign governments and corporations. Sector funds focus on the stocks of a *specific* industry or segment of the economy, such as energy, health sciences, utilities, or technology.

**Your financial professional can tell you more about mutual funds and discuss how investing in mutual funds could fit into your overall financial plan.**

*Mutual funds are sold by prospectus only. You should carefully consider the fund's investment objectives, risks, charges, and expenses before investing. The prospectus contains this and other information about the fund. For a current prospectus, contact your registered representative. Read the prospectus carefully before investing.*

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15 Corporate Circle, Albany, NY 12203  
800-525-4237 • Fax 518-862-3355  
www.newkirk.com • info@newkirk.com

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