FIN 366: INVESTMENTS
BRIEFING

Chapter 4: Mutual Funds and Other Investment Companies

Investment companies or **fund families** are financial **intermediaries** that pool and invest money on behalf of investors. They offer **mutual funds** or "**open-end" funds**, which are portfolios of securities that investors can collectively invest in, earning money in proportion to their investment amount. The **Net Asset Value (NAV)** is the value of a share in a fund, and aids in dividing the claims of the fund among its many investors. **Exchange traded funds (ETFs**) are similarly portfolios of securities, but investors purchase shares of ETFs on exchanges rather than directly transacting shares with the fund family. There are many types of mutual funds and ETFs, and in some cases, a fund can be more than one type: (1) **Money market funds** that invest in money market securities, (2) **Equity funds** that invest most of their funds in common stock, (3) **Sector funds** that invest primarily within one sector or industry, (4) **Bond funds** that invest in fixed income, (5) **International funds** that hold securities worldwide, (6) **Balanced funds** that invest in both equities and fixed income securities in stable proportions, (7) **Asset allocation funds** which similarly hold equities and fixed income, but vary proportions in each at the discretion of the fund's manager, and (8) **Environmental, social, and governance (ESG) funds** that are selective in their choice of investments based on the company's social goals. Funds may also be **active** (where managers choose securities to buy and sell) or **passive** (where managers invest in the securities by following some benchmark or index, also called **index funds**). Investing in mutual funds comes at a cost: (1) **Front end loads** may be charged when shares in the fund are purchased for the first time, (2) **Operating expenses** are charged annually, (3) **12b-1 fees** are charged annually to pay for marketing expenses of the fund, and (4) **Back end loads** are "exit fees" that may be paid to redeem your shares and cash out of the fund. The total of the annual fees charged is the fund's **expense ratio**. The fund's **prospectus** is a document that provides fund details. **Hedge funds** (*not* investment companies by the SEC's definition) are available to wealthy and sophisticated investors only, and may use leverage, short-selling, and speculative strategies, and hold illiquid securities.