INDEPENDENT INVESTOR

Strategies for Managing Your Assets

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Mutual Fund Categories: A Primer for New Investors

With thousands of mutual funds[1] available today, selecting the most suitable ones for your portfolio can be tricky business. Overwhelmed by the sheer number of funds, new investors understandably may be confused.

Included below is a summary of a number of common mutual fund categories. Once you have some understanding of the different fund categories -- which determine the kinds of securities that fund managers select for their funds -- the industry's seemingly endless differentiation may start to become clearer. You -- and your financial professional -- can then devise a mutual fund investment strategy that will work for you, bearing in mind your time horizon, risk tolerance, and ability to withstand fluctuations in the value of your portfolio.

- **Global** and **international funds** can help diversify your assets into a wide array of foreign stocks and bonds. The difference between the two groups is that global funds may buy a mix of U.S. and foreign stocks, whereas international funds invest exclusively overseas. Under the two fund groups, there are regional funds and country funds designed to take advantage of specific investment opportunities in the world's developed and emerging countries. In terms of risk ratio, global and international funds vary widely from lower-risk funds that invest in established markets to higher-risk emerging market funds. Be aware that investors in international securities may face additional risks (such as higher taxation, less liquidity, political problems, and currency fluctuations) that do not affect domestic securities.
- **Aggressive growth funds** are, as their name suggests, among the most aggressive equity funds. Aimed at maximizing capital gains, these funds invest in companies with the potential for rapid growth (such as companies in developing industries, small but fast-moving companies, or companies that have fallen on hard times but appear due for a turnaround). Some aggressive growth funds use several investment strategies in an effort to achieve superior returns. These funds can be very volatile in the short term, but in the long run they may offer the potential for above-average capital appreciation.
- **Growth funds** also strive for capital appreciation by investing in companies that are positioned for strong earnings growth. Funds in this group vary widely in the amount of risk they take. But in general, they are less risky than aggressive growth funds because they normally invest in well-established companies. Growth funds may entail less volatility than aggressive growth funds, but also less potential for capital appreciation.
- **Growth and income funds** strive for both dividend income and capital appreciation by investing in companies with solid records of dividend payments and capital gains. Some growth and income funds emphasize growth while others emphasize income. Growth and income funds may be less risky and less volatile than pure growth funds, but may also offer less potential for capital appreciation.
- **Sector funds** concentrate on one industry (such as technology, financial services, or consumer goods) or focus on certain commodities (such as gold, gas, or oil). Selected by more experienced investors who are willing to pay close attention to the market, sector funds are less diversified than the broader market and hence are often more volatile.
- **Balanced funds** offer one-stop shopping by combining stocks and bonds in a single portfolio. Balanced funds are more conservative than the previously discussed categories and usually invest in blue-chip stocks and high-quality taxable bonds. They may potentially hold up better in rough markets, because when their stock investments fall, their bonds may do well, and vice versa. Because they offer diversification, balanced funds are often suitable for people with a small amount of cash to invest.
- **Bond funds** can be divided into four broad categories: tax exempt, taxable, high quality, and high yield. Within these categories, funds are also segmented by maturities, type of issuer, and credit quality of bonds in which they invest.
- **Tax-exempt bond funds** buy bonds issued by state and municipal agencies, while taxable bond funds may invest in all other debt securities.
- **High-quality bond funds** stick with government and top-rated corporate or municipal bonds that offer relatively lower interest.
- **High-yield bond funds**[2] buy lower-rated or non-investment-grade corporate or municipal bonds, or

"junk bonds," which offer higher interest to compensate for the higher risks that investors take. While bond funds in general are less risky than stock funds, the return on principal is not guaranteed and bond funds have the same interest rate, inflation, and credit risks that are associated with the underlying bonds owned by the fund.

- **Money market funds**[3] invest in short-term money market instruments, such as U.S. Treasury bills, commercial paper, certificates of deposit, and repurchase agreements. Striving to maintain a stable share price of $1, money market funds offer increased safety and liquidity, as well as a yield that is generally higher than that of bank deposits, which unlike money market funds, are FDIC insured.
- **Allocation/lifestyle** and **target-date funds** may be another option for investors looking to simplify their choices. Allocation or lifestyle funds invest in a static mix of stocks, bonds, and money markets based on a particular risk profile.[4] **Target-date funds** also invest in a mix of asset classes, but that mix changes over time as you approach the target date, typically your expected date of retirement. For example, a 2040 fund might feature a mix of stocks and bonds that gets progressively more conservative as you approach year 2040 and beyond. Note that the principal value of a target date fund cannot be guaranteed at any time, including the target date, and may decline at any time.

Which mutual fund categories will best meet your investment needs will depend on a number of factors, including your investment time horizon and your tolerance for risk.

[1]*Investing in mutual funds involves risk, including loss of principal. Mutual funds are offered and sold by prospectus only. You should carefully consider the investment objectives, risks, expenses and charges of the investment company before you invest. For more complete information about any mutual fund, including risks, charges, and expenses, please contact your financial professional to obtain a prospectus. The prospectus contains this and other information. Read it carefully before you invest.*

[2]*Lower-quality debt securities involve greater risk of default or price changes due to changes in the credit quality of the issuer. They may not be suitable for all investors.*

[3]*An investment in a money market fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency. Although the fund seeks to preserve the value of your investment at $1.00 per share, it is possible to lose money by investing in the fund.*

[4]*Asset allocation does not ensure a profit or protect against a loss in a declining market.*

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