

Mutual Funds 101



What they are and how they can help build your wealth.

If you've never invested before - or have all of your investments held by your employer - you may not know much about mutual funds.

Canadians have been investing in them since the 1930s, but they're still a mystery to many people. We take a look at how mutual funds work, their pros and cons and whether they might be the right investment product for you.

So, what are mutual funds?

A mutual fund is like a collection of investments that can include stocks, bonds and other assets. Other investors also buy into the fund, so it gives you access to a greater range of investments than you could afford on your own.

Owning a mutual fund that contains potentially hundreds of assets is one of the easiest ways to diversify your investments. And diversification is really important for any investor.

Why investment diversification matters

Diversification minimizes the risks of investing in the stock market. Let's say you own shares in five companies. If one goes under, that would have a huge impact on your savings.

By investing in mutual funds, however, you get to own a slice of dozens of companies. If one of them goes bankrupt, the impact would be far smaller.

It's also important to diversify in other aspects of your portfolio, for example, the size of the companies, the industry and the region. This reduces the risk of taking heavy losses if a particular industry or a region's economy collapses.



Types of mutual funds

Some of the main types of mutual funds:

Money market funds invest in typically safe fixed-income securities, such as treasury bills, but provide low returns.

Fixed income funds focus on investments that pay a fixed rate of return, (e.g., bonds), with low risk and low returns.

Equity funds are made up entirely of stocks, so they can be a riskier proposition, but with a higher potential for growth.

Asset allocation or balanced funds carry a mixture of fixed income and equity funds, to try and balance risk and return.

Index funds aim to track the performance of specific indexes, such as the Toronto Stock Exchange.

Specialty funds focus on specific industries or investment philosophies.

The benefits of mutual funds

- An easy way to create a diversified investment portfolio and therefore reduce risk
- Allow you to own shares in a greater number of companies
- Easy to buy, with low minimum investments
- You can invest with a lump sum or monthly payments
- You don't pay transaction costs for each individual stock
- Usually easy to sell, so you can get your hands on your cash fairly quickly
- Funds are managed by investment professionals, with more knowledge and experience than the average personal investor
- Traded only once daily, so they don't fluctuate with the market during the trading day

Disadvantages of mutual funds

- Some mutual funds perform worse than the market, so do your homework
- If funds are in a non-registered account, you'll pay taxes on any capital gains if any stocks in the fund are sold for more than their purchase price
- Some mutual funds have high sales charges and management expense ratios, which can greatly reduce your investment growth

What are the best mutual funds for you?

This will depend on the amount you want to invest, your timeline and your risk tolerance. Long timelines can afford riskier funds with higher potential returns, because there's time to recover from any market dips.

If the stock market rollercoaster worries you, you might prefer funds containing a higher percentage of bonds. If you have high-risk tolerance, funds with a high percentage of stocks might be a good choice.



A Cornerstone financial advisor can advise you on the best mutual funds for your investment goals and risk tolerance.

Call **1.855.875.2255** today to book an appointment.

