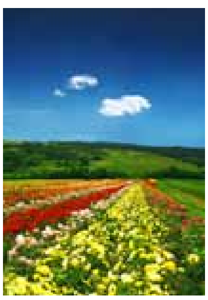
Wealth Management Education Series

Standard Chartered
Here for good

Explore the Field of Investment Funds

Managing your wealth well is like tending a beautiful formal garden – you need to start with good soil and a good set of tools. Just as good soil has the proper fertility to nourish a plant, having the right foundation in financial literacy should empower you to potentially cultivate a successful investment portfolio. ***Explore the Field of Investment Funds*** is part of our **financial education series** to help educate you on the fundamentals of investing as you tend your very own financial garden.



What are Investment Funds?

Investment funds is a general term for funds that allow you to pool your money with that of other investors and are managed by a team of investment professionals. The term may vary across countries but investment funds may also be referred to as **collective investment schemes**, unit trusts or simply as funds.

The pooling of your money generally creates **greater buying power** so you are able to invest in a **wider range of investments** than possible for most individual investors. Each investor in a fund owns units (or shares) which represents a part of a fund's portfolio holdings.

Investment funds can be categorised by the type of assets they invest in (such as shares, bonds, cash or other securities). You can refer to the Investment fund's prospectus and factsheets to get a better understanding of their respective investment objectives and policy (for example, type and mix of investments) and past performance.

Investment funds are *open-ended* funds but some investment schemes are structured as closed-end funds (see page 16). This document is focused on open-ended investment funds.

Open-ended funds - can issue and redeem units at times specified to meet subscription or redemption requests made by investors. The price per unit of an open-ended fund will vary to reflect the fund's performance.

The price per unit of an open-ended fund is known as its net asset value or NAV.

This is calculated as follows:

$$\frac{\text{Fund's assets} - \text{Fund's liabilities}}{\text{Number of units issued}}$$

What are the Fees?

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Investment funds charge various fees and it is best to refer to the fund's prospectus to understand what you are being charged.

Examples of the type of fees that may be charged:

Front-end fee / subscription charge

It is deducted directly from the subscription amount or reflected from the fund's offer price or net asset value (NAV).

Management fee

Typically charged to the fund to pay the investment manager of the fund.

Custodian / trustee fee

Typically charged to the fund to pay for services provided by a custodian or trustee of the fund.

Any fees that are charged to the fund is paid out of fund assets and will be indirectly borne by the investors. Investor should refer to fund prospectus for details.

What Types of Investment Funds are there?

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There are many types of investment funds, but broadly speaking they can be divided into four main categories:

1. **Equity (Stock) Funds**
2. **Bond (Fixed Income) Funds**
3. **Money Market Funds**
4. **Hybrid Funds**

Equity (Stock) Funds

1

As the name suggests, Equity Funds consist mainly of stock investments and are the most common type of investment funds. Often Equity Funds focus on a particular type of investment strategy, such as Growth, Value, Large Caps, Small Caps or themes such as Property, Energy, Healthcare. The funds can be invested globally, regionally or in single countries.

Bond (Fixed Income) Funds

2

As the name suggests, invest mainly in debt instruments including government bonds, corporate bonds or high yield bonds. The return that a Bond Fund may have can vary depending on the type of bond. Typically, Bond Funds that invest in government bonds tend to be less volatile. Bond Funds that invest in corporate or high yield bonds generally do so to obtain higher yields, thus carrying greater risk.

Money Market Funds

3

Money Market Funds seek to maintain a stable net asset value by investing in the short-term, high-grade securities sold in the money market. These are generally the safest, most stable securities available, including Treasury bills, certificates of deposit and commercial paper.

Hybrid Funds

4

Hybrid Funds invest in a mix of stocks and bonds and may also hold money market instruments which can vary proportionally over time or remain fixed. They may be further sub-divided into Balanced Funds and Asset Allocation Funds.

What are the Benefits?

Diversification	Investment funds can give you instant diversification. With as little as HKD1,000 you can buy a fund which invests in equity and bond markets around the world. The investment risk is spread over many securities, thus potentially reducing the volatility of your portfolio.
Active, Professional Management	You can enjoy professional management when you invest in an investment fund. The investment professionals will manage the funds on your behalf using their experience, skills and resources.
Liquidity	Generally, for investment funds that are daily priced and open-ended, you can redeem your units any day and get your money back promptly.

What are the Risks?

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When you invest in a fund, you should receive the fund offering document which include a fund prospectus, which will detail the risks involved in investing in the investment fund. We have outlined examples of general risks relating to an investment in an investment fund, but it is important for you to review each prospectus in detail so that you are aware of all the risks you may incur for any particular investment fund.

Market Risk

This is the risk that the value of an investment fund's investments may fluctuate in response to broader market movements – for example, in the stock or bond markets. In addition, the market price (net asset value) of investment funds themselves may fluctuate in response to volatility in their component investments.

Currency Risk

If an investment fund invests in overseas securities, this is the risk that any adverse foreign exchange movement in the currencies of denomination of these securities against the investment fund's own reporting currency will have a negative impact on the investment fund's net asset value.

Investment Objective Risk

This is the risk that your objectives will not be met by investing in the investment fund.

Due to the specific features of different investment funds, hence, investors should read the Risk Disclosure Statement (RDS) before invest.

What Other Types of Investment Funds are there in the Market?

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1 Closed-End Funds

These funds issue only a fixed number of units or shares, and do not issue new units or shares even as investor demand grows. Unit or share purchases take place in the secondary market, and prices are determined by investor demand. Units or shares of these funds are often traded at a premium or discount to the fund's net asset value.

2 Index Funds

An index fund is passively managed and is not listed on a stock exchange. It is designed to replicate the return of a broad market index such as the S&P 500 by buying the index's component stocks.

3 Exchange-Traded Funds

An Exchange-Traded Fund (or “ETF”) is a security traded on a stock exchange that tracks a market index (such as the S&P 500). An ETF may track the same underlying market index as an Index Fund, but there are still differences between the two. The key difference is that ETFs are openly traded in a stock exchange throughout the trading day and can be purchased in small / flexible investment sizes through a brokerage account. In contrast, you can generally only redeem out of an Index Funds at the end of the day, at the prevailing price (NAV) of the fund.

4 Hedge Funds

Hedge funds are another type of investment funds; they undertake a wider range of investments and trading activities than investment funds. For instance, hedge funds can invest in options, futures and even operating businesses. They can also take on short-sell positions and highly-leveraged transactions – both of which are generally not allowed for investment funds.

Hedge funds generally aim to achieve higher absolute returns in all market conditions for their investors.

Difference between a stock...

When you own shares of an **individual stock**, you are in effect, a direct owner of that company. By owning a stock you also assume the risks associated with that one company. For example, if that company goes bankrupt, you can lose all your investment in that stock. If you have a strong view about a particular stock and the direction of the stock market, you can potentially profit by trading the stock.

...and an investment fund

When you own a share of a **fund**, you are pooled together with other investors and own a share of a portfolio comprising many stocks. This can help diversify the stock holdings and reduce the risk associated with individual stock ownership. Moreover the fund is managed by a professional manager who decides what stocks to buy and what stocks to sell, that is, the manager makes the trading decisions on behalf of unitholders.

Investment funds are designed for longer-term holding rather than short-term trading. In fact short-term trading by unitholders can hurt fund performance due to higher transaction costs borne by the fund in order to unwind positions at possibly unfavourable times to meet frequent redemption requests.

What do these Investment Terms mean?

Alpha

A measure of selection risk of a fund in relation to the market. A positive alpha is the return awarded to the fund manager for taking a risk, instead of accepting the market return. For example, an alpha of 0.4 means the fund outperformed the market-based return estimate by 0.4%.

Arbitrage

Arbitrage can be described as a technique of simultaneously buying a security at a lower price in one market (for example, cash market) and selling at a higher price in another market (for example, futures market) to make a profit on the spread between the prices.

Beta

A measure of sensitivity of your investment to market movement.

A beta of 1	indicates that the investment should move in line with the market.
A beta of less than 1	means that the investment should be less volatile than the market.
A beta of greater than 1	indicates that the investment should be more volatile than the market. For example, if a stock's beta is 1.2, it is theoretically 20% more volatile than the market.

Information Ratio

A statistical ratio which is a measure of the consistency of the excess return or value-added by the investment manager. It aims to measure the value that has been added by a manager per unit of risk taken relative to the benchmark. All else being equal, the higher the information ratio, the better.

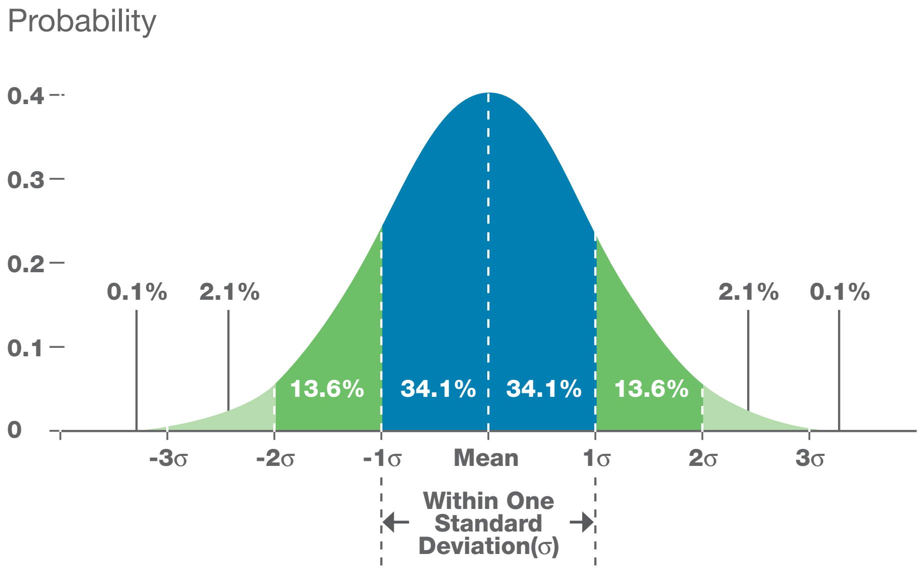
Sharpe Ratio

A ratio to measure risk-adjusted performance. It is calculated by subtracting the risk-free rate (deposit rate) from the rate of return for a portfolio and dividing the result by the standard deviation of the portfolio returns. The Sharpe ratio tells us whether the returns of a portfolio are due to smart investment decisions or a result of excess risk taken by the manager.

Standard Deviation

Measures the dispersion of a series of returns from the mean return. When returns are normally distributed, an individual return will fall within one standard deviation of the mean about two-thirds of the time. For example, if your investment has an average return of 8% and a standard deviation of 10%, then it means that 68% of the time the return was between – 2% (8% less 10%) and 18% (8% plus 10%).

Theoretically, the higher the standard deviation the higher the investment risk.



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Would you like to have a further discussion on this subject?

Contact your Relationship Manager, or any of our Standard Chartered Bank locations closest to you for more information.

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