ACTIVITY 6.1
CLASS INVESTMENT CLUBS

The members of your class have decided to form investment clubs. Class members may buy as many shares in a club as they like, for $10 per share. Each club sold 300 shares and collected $3,000. Now it's time to invest the money.

Your club held its first meeting and decided to invest in stocks. The club members proposed different stocks to buy. Here is a rundown on the stocks proposed.

1. American Cellular, $5 per share

This is a new cellular company that features high-tech services such as advanced video. So far, the company has not made a profit, but it expects to do very well soon.

2. Big Box Stores, $20 per share

Big Box Stores is one of the leading discount retailers in the country. Same-store sales have increased steadily in each of the last five years.

3. Biotech Industries, $10 per share

Biotech Industries is a pharmaceutical company that specializes in developing cutting-edge drugs. It has some profitable products, but so far its profits are small.

4. General Grocery, $20 per share

This is a leading grocery store chain. Sales are generally steady and do not change much with the economy's ups and downs. However, some experts predict that the growing trend toward eating out in restaurants will hurt future sales.

5. Giant Auto, $10 per share

Giant Auto is one of the three leading automobile manufacturers in the world. The company's profits depend on economic conditions. Profits are high in times of strong economic growth and poor in bad times or recessions.

6. Gold Mining Group, $5 per share

GMG is a gold-mining company. The price of gold often rises in bad times or recessions and falls in good times.

Your club decided to invest all 300 shares or $3,000 in at least three of these companies. Decide how to invest the money, and record your investments in Table 1.

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Table 1: Making Investment Choices

Company	Price per Share	No. of Shares Owned	Amount Invested
American Cellular			
Big Box Stores			
Biotech Industries			
General Grocery			
Giant Auto			
Gold Mining Group			
Total Investment Value (add last column)			

Number of shares 300 *Price per share $10

**The price per share is the amount invested divided by the number of shares.*

ACTIVITY 6.2
A CLASS INVESTMENT CLUB ONE YEAR LATER

One year later, the prices of your investments have changed. The price per share of each investment is listed in Table 1 below.

Complete the chart to determine how well your investment club did. The value of your investment depends on the companies in which you invested.

Table 1: One Year Later

Company	Price per Share	No. of Shares Owned	Amount Invested	Investment Value 1 Year Later
American Cellular	$8			
Big Box Stores	$23			
Biotech Industries	$8			
General Grocery	$22			
Giant Auto	$11			
Gold Mining Group	$4			
Total Investment Value (add last column)				

Number of shares 300 *Price per share ___

**The price per share is the total investment value (one year later) divided by the number of shares.*

ACTIVITY 6.3
MUTUAL FUND FACTS

A mutual fund is a pool of money similar to the money collected by a class investment club. A fund manager decides how to invest the money, with the goal of increasing the value of each share of the fund for the investors. That will happen only if the value of the investments chosen by the fund manager increases.

Investors may buy shares of open-end mutual funds each business day for the net asset value (NAV, in the fund listing), the investment value of each share. The net asset value is calculated each day by dividing the total value of the investments by the number of shares. This is how you calculated the value of the shares of your investment club. You may also sell your shares in an open-end mutual fund on any business day and receive the NAV.

More Americans invest through mutual funds than by any other investment method. There are thousands of mutual funds. There are stock mutual funds, bond mutual funds, stock and bond mutual funds, and money-market funds. There are mutual funds that specialize in almost any type of stock or bond. Some mutual funds, called index funds, buy the stocks that allow investors' returns to match a particular index—for example, the Standard & Poors Index of 500 large stocks. Index funds can provide more diversification than actively managed funds. In addition, the management fee of an index fund (discussed later) should be lower because the fund manager does not have to research which stocks to buy and sell. For this reason, many experts advise buying a fund that tracks a broad market index if only one fund is bought.

Some mutual funds buy high-risk investments and some buy low-risk investments. How can you choose the right mutual fund? Here are some factors to consider.

1. **Performance.** Buy mutual funds that you believe will perform well. Performance is the most important factor to consider. However, your consideration of performance must be tempered by how much risk you are willing to take. A mutual fund prospectus lists the stocks or bonds a fund owns and provides information on the fund's performance. But past performance does not guarantee that the fund will do as well in the future. The fund manager is a key to a fund's performance. It is a good thing if the fund manager has had favorable results and has worked for the fund for a significant period of time.

2. **Cost.** A mutual fund company makes money by charging investors various fees. These fees are a cost to investors. The lower the costs, the better it is for investors—as long as performance is strong. Here are some typical costs of mutual funds:

   - Some funds charge a *load*. A load is a sales commission. It is usually a percentage of the price, and it can be as high as 8 percent. A front-end load is paid when you buy shares, and a back-end load is paid when you sell shares. A no-load fund does not charge a sales commission. If you need help in choosing a fund, you might consider paying an investment advisor a load or commission for advice. If you do not need help, choose a no-load fund.

   - All funds charge a *management fee* and have *expenses*. The lower the management fee and the expenses, the better it is for investors.

- Some mutual funds charge a *12b-1 fee*. This fee, which can be as high as 1 percent of the fund's value, is used by the company to advertise the fund to the public. Unless the fund has great performance, it is better to avoid funds with 12b-1 fees.

3. **Convenience.** A fund that provides good service is very helpful to investors. Are the statements easy to read? Are the fund's service representatives knowledgeable and helpful? Is it easy to make additional investments in the fund? Can you buy small amounts of the fund? Can you exchange shares in the fund for shares in another of the company's funds? Some fund families have dozens of different funds for different investment objectives.

Advantages of Investing in Mutual Funds

Why buy a mutual fund? After all, you can buy stocks and bonds directly. Many investors find that buying mutual funds provides several advantages over buying individual stocks and bonds. These advantages can make the extra costs worthwhile.

1. **Professional management.** When you buy a mutual fund, a professional money manager chooses your stocks. The performance of your investment club depended on which stocks you bought. A professional manager might be able to make these choices better than you can. If you don't think this is true, you can buy an index fund. An index fund follows a stock average, attempting to match the performance of the average. For example, a Standard & Poors 500 Index fund can simply buy all 500 stocks that are in the index, in that way seeking to match the index's performance. The investor gets average performance. Over the years, a majority of actively managed funds have failed to beat average performance.

2. **Diversification.** *Diversification* means you spend your money on several stocks and bonds rather than just a few. If one or two stocks or bonds in your mutual fund decrease sharply in value, your loss will be less than if you own only a few stocks or bonds. If a class investment club bought only one stock, it could have a greater loss or greater gain than if the club bought several stocks. Your risk is greater the fewer stocks you buy. A mutual fund may own 500 or more different stocks.

3. **Liquidity.** *Liquidity* refers to the ease with which an asset may be exchanged for cash. A home is usually a valuable asset, but it is not a highly liquid asset because it cannot be exchanged for cash until the owner succeeds in selling it, which may take some time and effort. A mutual fund, by contrast, is a highly liquid asset. If you own shares in a mutual fund, you can sell your shares at the net asset value (NAV) on any business day. Of course, you may need to sell the fund for less per share than what you paid for it, and lose money.

4. **Investment objective.** There is a mutual fund for almost any objective or goal. When you determine your goals and the risks you are willing to take, you can probably find a mutual fund that matches them.

Questions for Discussion

A. What is a mutual fund?

B. A friend tells you, "All mutual funds are the same." How do you reply to your friend?

C. What is an advantage of buying a load fund? What is a disadvantage?

D. What is an advantage of buying a no-load fund? What is a disadvantage?

E. What should you consider when deciding which mutual fund to buy?

F. More Americans own mutual funds than individual stocks and bonds. Why do you think this is so?

G. If your class participates in a stock market simulation that allows you to buy mutual funds, what type of fund should you buy? Why?

H. What are the advantages and disadvantages of buying index mutual funds rather than actively managed funds?

I. If you want to buy a mutual fund so that you will have money to buy a house 10 years from now, what type of fund should you buy? Why?

ACTIVITY 6.4
A MUTUAL FUND PROSPECTUS

1. All mutual funds must supply potential investors with a prospectus. A prospectus is a document that provides information about the fund's investment objectives, investment strategy, past performance, costs, and other charges. The bullet points below present excerpts from one fund's prospectus. Read the excerpts, including the table showing **Average Annual Total Returns.**

   - The fund is an aggressive stock fund seeking long-term capital growth primarily through investments in small, rapidly growing companies.
   - Investing in smaller companies generally involves greater risk than investing in larger companies. Stocks of small companies are subject to more abrupt or erratic price movements than the stocks of larger companies.
   - The fund is 100 percent no-load. There are no 12b-1 fees.
   - The fund's annual management fee and other expenses are .91 percent. These expenses are deducted from the fund's assets.
   - The table below summarizes the fund's average annual returns for one year, five years, and 10 years.

Average Annual Total Returns

Fund Intervals	1 year	5 years	10 years
Returns before taxes	-2.84%	8.07%	13.75%
Returns after taxes on distributions	-3.33	6.37	11.03
Returns after taxes on distributions and sale of fund shares	-1.30	6.27	10.56
Russell 2000 Growth Index	-9.23	2.87	7.19
Russell 2000 Index	2.49	7.52	11.51
S&P 500 Stock Index	-11.89	10.70	12.94
Lipper Small-Cap Fund Index	-9.32	6.45	10.29

2. Then use your understanding of the prospectus to answer the following **Questions for Discussion:**

   A. You worry a lot about the stock market and want to limit the risk of losing your money. Would you buy this fund?

B. Does this fund charge a sales commission?

C. Is it good or bad for investors that this fund charges no 12b-1 fees?

D. How much does this fund charge in fees?

E. In your opinion, how does the fund's past performance look?

F. Does this mean the fund will perform well in the future?