INVESTMENT BANKING, OPEN, CLOSED END, FUNDS

Investment Banking companies are financial intermediaries that sell shares to the public and invest the proceeds in a diversified portfolio of securities. Each share sold represents a proportional interest in the portfolio of securities managed by the company on behalf of its shareholders. The type of securities purchased depends on the company's investment objective.

Types of investment companies
1) open-end funds (mutual funds)
2) closed-end funds
3) Unit Trusts

Open-end funds (mutual funds) — These are portfolios of securities, mainly stocks, bonds and money market instruments.

Important aspects
1) Investors own a pro-rata share of overall portfolio.
2) Investment manager of fund manages the portfolio actively (i.e., buys some, sells some securities)
3) Value or price of each share of portfolio called NAV (net asset value) = Market Value of portfolio - liabilities
4) NAV is determined once every day at close of day
5) All new investments into fund and withdrawals from fund during a day are priced at closing NAV.
6) Total no. of shares in fund is influenced if there are more investments than withdrawals during the day, and vice versa.
7) If prices of securities in portfolio changes, both unit size of portfolio as well as NAV changes.
8) NAV will vary with change in price of securities in portfolio.
Closed-end funds: "Closed stocks of corporations"

New shares of closed-end funds are entirely issued by an underwriter for the fund. After new issue no of shares remains constant. After initial issue no sale of purchase of fund shares by fund company.

Shares no trade on secondary market, either on exchange or OTC market.

Prices are determined by demand/supply on secondary market.

Shares selling below NAV— at discount.

Above NAV— at premium.

Initial investors have to pay substantial commission.

Proceeds from managers of funds have to invest equals fee paid by initial buyers of shares + cost of issuance Cost + 7.5% of total.

Includes selling fees or commissions, paid to retail brokerage firms, that sell stock.

More popular.

(ETFs — hybrid closed-end vehicles, which trade on exchanges, very close to their NAV,  
Cost to investor is similar cost of stock of corporate stock divided by shares, commission, bid/offer spread is also a cost.)
Sale Price of Unit = (Marked value of asset - liabilities) + (Carr + Thrift + Capital gains & mortgage expense)

Re-Purch. Price = __________ - (Brokerage + Clearing cost/Comm. et al)

R. of return
R.R.U. = \( \frac{\text{NAV}_t - \text{NAV}_{t-1} + \text{Dividends + Capital gains}}{\text{NAV}_{t-1}} \)

Advantages:
- Economies of scale
- Spread trading
- Liquidity
- Flexibility
- Tax benefits
- Wide choice of schemes
- Freedom for churn

To finance growth - issue of bonds for stock.

Long term holding

Take into consideration capital gains along with income dividends.
Unit Trust
No. of Unit Certificates is fixed.
Unit trusts invest in bonds.
There is no active trading of bonds in the portfolio of
Trustee holds all the bonds till redeemed by issuer.

But it may sell an issue in the portfolio of
trustee is dramatic downfall in issuer's credit
quality.

Cost of operating a trust is considerably less.

Unit trusts have a fixed termination date.
All unit trusts charge sales commission (3.5%)

Costs borne by investor

Fund Sales Charges and Annual Operating Expense

Shareholder fee

In sales charge

Operational expenses

One time cost

Imposed annually

Sales charges

Two types of sales charges dependent on

Methods of distribution

Sales force

Wholesale

Direct

lt investor

No load

divid end is bought at NAV

ie to another, ins. agent etc.

Sales charge in such cases is called a load.

Front end load = at time purchase

Back end loads = at sale

Level loads = imposed uniformly

each year


Annual Operating Expense (Before Reh.)

Management fee \[\rightarrow\] Dist. fee \[\rightarrow\] other expenses \[\rightarrow\] Costs of
1) Custody
2) Transfer Agent
3) Independent Public Accountants' fee
4) Directors' fee

\[
\text{Sum of management fee + Dist. fee + Other Annual expenses} \rightarrow \text{Expense Ratio}
\]

Types of funds

By investment objective
- stock funds, bond funds, money market funds
- passive
- active funds

Passive
- V (indexed)
- designed to replicate an index
- stock funds

Active funds
- try to outperform index

Fund of Funds
- invest in funds

Family of funds or CEF or complex of funds
- management offers choice of investing in funds built different investment objective

On basis of M-Cap
- Small: not \$2 billion
- Mid: \$2 to \$12 billion
- Large: > \$12 billion

Stock Style
- Growth - high price to earnings ratio
- Value - low

Sectors
- specialize in any one sector

Market capitalization is equal to the share of a company at a pt. of time multiplied by outstanding shares.