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The Types of Mutual Funds

In theory, the types of mutual funds are endless. They vary depending on the types of securities, businesses or assets in which the funds invest. Most retail mutual funds are open-end. By way of example, at the fundamental level, there are four varieties of open-end mutual funds which are categorized by their risk and returns:

1) Money market funds are a highly liquid type of mutual funds that invests solely in money market instruments or short-term (normally less than a year) debt securities of agencies of the U.S. Government, banks and corporations, such as Treasury Bills, certificates of deposit, and commercial paper. It is a type of mutual funds the price of which does not fluctuate much in value. The main goal is the preservation of principal, accompanied by modest dividends.

2) Fixed-income funds (normally bonds) invest mostly in long term (from 1 year to 10 years) fixed income securities. This type of mutual fund carries more risk than money market funds and is often used to produce income or to help stabilize a portfolio (diversification). Fixed-income funds are such as Corporate Bond Funds and Mortgage-Backed Securities Funds.

3) Equity funds (stocks) are, as the name suggests, made up of investments of common stock or equity securities. Since stocks are risky, these funds can be riskier than other types but their chance of return can also be higher. Since company stocks are often categorized by their capitalization (or market cap), and come in three basic sizes: small, medium, and large. Many mutual funds invest primarily in one of these sizes and are thus classified as large-cap, mid-cap, or small-cap funds. Additionally, mutual funds are sometimes categorized by the nature of stock that is bought and their growth potentials. These funds types are then generally described as "growth", (high risk, high return) "value" (low risk, stable growth) or a combination of the two, called "blend." The least risky is “guarantee” funds, which assures investors that they will not lose their capital, but

as the investment manager needs to preserve the assets to ensure that the capital can never be lost, it is usually very conservative and the return is also low.

4) Balanced funds are a type of mutual fund that buys a combination of money market funds, fixed-income funds and equity funds to provide both income and capital appreciation while avoiding excessive risk. Such diversified holdings ensure that these funds will manage downturns in the stock market without too much of a loss; the flip side is that balanced funds will usually increase less than an all-stock fund during a bull market.