

# SeeWhy Financial Learning's ~ IFIC Exam Preparation Materials ~

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Here at SeeWhy Financial Learning, we have a knack for making difficult concepts seem easy. After hearing a topic explained properly by one of our trainers, our students often say, “Why doesn’t the textbook just teach it that way?” Frankly, we don’t know why, so we started our own company!

Our IFIC Exam Preparation Success Package provides you with study tools to speed up your learning and ensure that your first exam attempt is a successful one. This package is so effective that it comes with a money back guarantee. In the unlikely event that you do not pass, we will refund your money!

The success package includes:

- Key Concept Flash Cards (online – free sample on our website)
- Realistic Practice Exam Program (online – free sample on our website)
- Textbook Summary Study Guide

The Textbook Summary study guide:

- ✓ Simplifies the IFIC® textbook using everyday language, memory aids and analogies
- ✓ Contains approximately 100 IFIC® practice questions
- ✓ Significantly reduces IFIC® study time

You can try our exam preparation software for free on our website. The following will give you a feel for how we simplify concepts in our Textbook Summary study guide.

## **Easy To Understand Text Book Summary**

Our study notes read very much like we teach in a class room setting. They are informal, use everyday language, give you insight as to what is most important for the exam, and use memory aids. All of this makes the learning easier. The following are some excerpts from our IFIC® Textbook Summary Study Guide.

### **Introduction**

If you were taking a course on auto mechanics, it would seem backwards if your teacher started teaching you how to re-build a transmission before establishing that you actually know *what a car is*. Strangely, many mutual fund textbooks do just that; they begin by telling you how the mutual fund industry is regulated, the required disclosure documents on mutual funds, rules surrounding how mutual funds are sold, and only then tackle the issue of just what a mutual fund is. Here at SeeWhy Financial Learning, we feel that this doesn't make any sense.

For the most part, our study notes will follow the flow and order of the actual textbook, with one exception: *the beginning*. So let's start at what should be the beginning -- a discussion on what a mutual fund is.

### **Just What is a Mutual Fund?**

Consider the following scenario:

Amanda has \$3,000 in her bank account to invest. She knows she will not need the money for several years and that she would probably earn a greater return if she invests in the common shares of some good quality companies. What issues could she face?

1. She may not be comfortable selecting which stocks to buy;
2. If she is comfortable selecting the investments, she may not have the time to do the required research;
3. She doesn't have sufficient money to buy enough different stocks to properly diversify her portfolio (spread out her risk).

Investing in a mutual fund solves all of these problems.

The following bullet points will help you understand how mutual funds work:

- A mutual fund is a big pot of money and investors contribute to the pot.
- Each investor obtains units of the fund (like shares) based on how much money they contributed.
- The fund manager uses the money in the pot to invest, and is paid a management fee for his professional services.
- Once you have selected an appropriate fund or group of funds, you can sit back and let the fund manager do his or her job.
- Investors profit or lose based on how the fund performs, and how many units they own. For example: If the fund earns \$100,000 in income, and you own 5% of the fund's units, you will receive \$5,000 (5% of \$100,000).

### **Mutual funds offer many advantages:**

- |                                                |                                                                                                                                                  |
|------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Professional management:</b>                | • A professional money manager invests the assets.                                                                                               |
| <b>Cost savings for investors:</b>             | • The fund will pay lower commissions when buying investments since the fund buys in bulk.                                                       |
| <b>Diversification:</b>                        | • A large equity fund may hold shares in 60 to 100 different companies.                                                                          |
| <b>Variety of funds / transferability:</b>     | • Each fund family usually has several types of funds. They will also allow you to transfer from one fund to another.                            |
| <b>Variety of purchase / redemption plans:</b> | • You can invest a lump sum or by periodic investments such as monthly PAC plans. PAC stands for Pre-Authorized Contribution.                    |
| <b>Liquidity:</b>                              | • Most funds allow you to redeem your units at the next valuation point.                                                                         |
| <b>Ease of estate planning:</b>                | • The funds can continue to be invested during the whole probate process right up until the funds are ready to be paid out to the beneficiaries. |
| <b>Loan collateral:</b>                        | • Mutual funds can be given as collateral for a loan.                                                                                            |
| <b>Eligible for margin:</b>                    | • Many investment companies will give you a loan based on the value of your funds.                                                               |

**Exam tip!** If you are asked what the **main advantage** of mutual funds is, the answer is “**professional management**”.

**Mutual funds do have some disadvantages:**

**Costs:**

- Most mutual funds charge a sales commission and all charge a management fee.

**Unsuitable as a short term investments or emergency fund:**

- Due to the nature of the investments that mutual funds invest in, they are not suitable as a short-term investment. The exception is money market funds.

**Professional investment management is not infallible:**

- Even a professional money manager can make some poor investment decisions.

**Tax complications:**

- Any income earned by the fund must be paid out to unit holders each year. The unit holders must pay the applicable tax annually. Unlike owning an individual common share where you can decide if and when you sell it (thereby triggering a capital gain or loss), a mutual fund unit holder has no control when capital gains are triggered.

## Basic types of Mutual Funds

There are many different types of mutual funds, ranging from ones that are very safe (such as money market funds) to very risky funds (such as specialty funds).

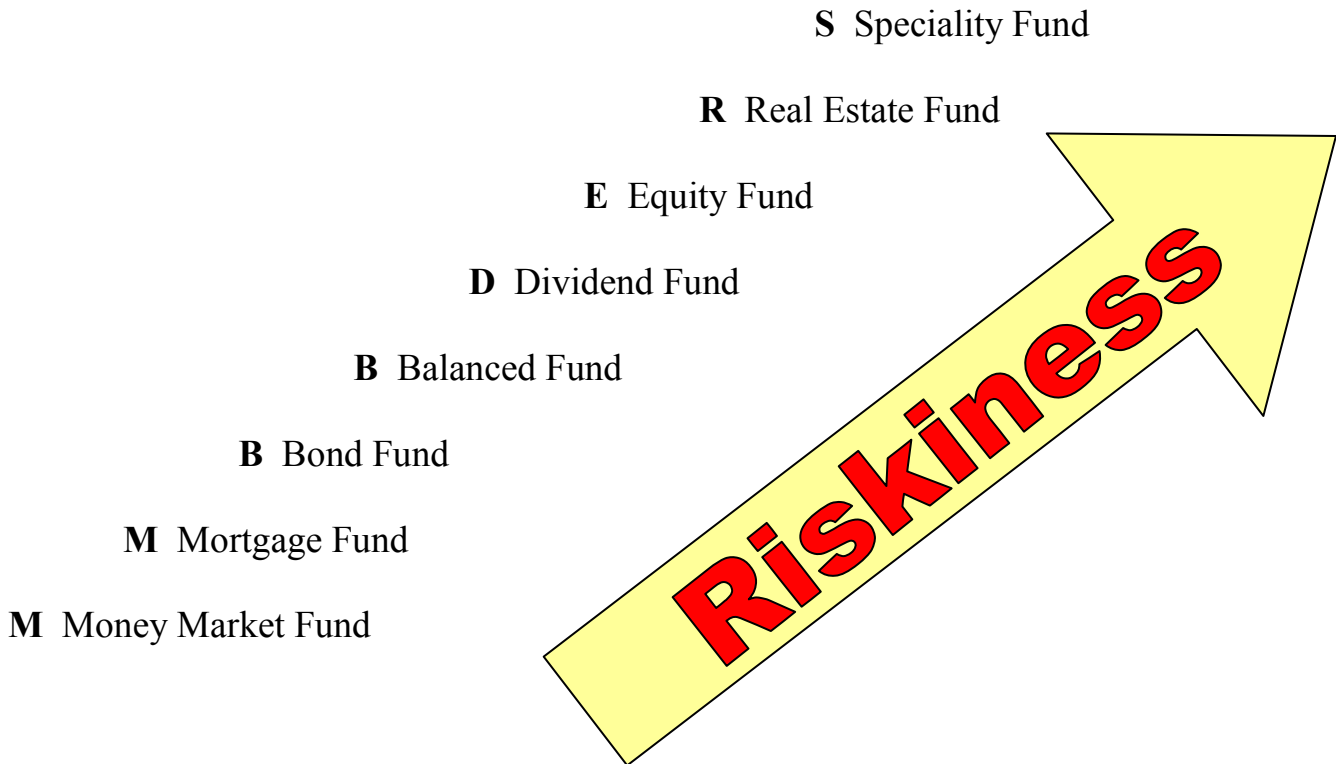
Each fund type is explained here at a very high level, as they will be discussed in much more detail in a later chapter.

- Money market:**
- Invests in safe investments such as government issued treasury bills, short-term commercial paper, banker acceptance paper and government of Canada bonds with terms of three years or less.
- Mortgage:**
- Invests in conventional mortgages or mortgages which are secured by Canada Mortgage Housing Corporation.
- Bond:**
- Invests in corporate or government bonds.
- Balanced:**
- Invests in all three asset classes namely money market, fixed income and equities. The manager will adjust the asset mix according to what he feels the outlook is for each asset class. If he feels equities will do well he will shift the portfolio closer to equities. If he feels bonds will do well he will shift the portfolio towards bonds.
- Dividend:**
- Invests in preferred shares and the common shares of blue chip companies that historically pay a stable dividend.
- Equity:**
- Invests in common shares.
- Real Estate:**
- Invests in real estate (usually commercial real estate).
- Specialty:**
- Very specialized funds that invest in things like precious metals, oil and resources, etc.

**Note:** Do not be alarmed if you don't know what a bond, money market instrument, or even a mortgage is. They will be discussed in detail as we move through the textbook summary.

To remember the risk level of the various funds, use the following memory aid:

**“My Mortgage Broker Brought Down Every Rate Substantially”.**



## Fees and Charges

Mutual funds sound great, right? Unfortunately, anything great usually comes at a cost. There are two basic types of fees that mutual funds charge:

### Sales commissions & Management Fees

**Management Fees:** All mutual funds charge a management fee because all mutual funds have a fund manager. A fund manager doesn't work for free! Management fees range from 0.5% to 3.0% of the net assets managed per year.

The management fee is be higher for an actively managed fund because they are more work for the fund manager. For example, if it's an index fund (simply copies an index) it is not actively managed and will charge a low management fee. On the other hand, if the fund's objective is to try to outperform the market, it will have to be actively managed and will charge a higher management fee.

### Sales Commissions (Loads):

**No Load:** Do not charge a sales commission (load) at all. These are usually "in-house" mutual funds sold at a bank.

**Front-end load:** A commission is charged when you buy the fund.

**Back end load** (also known as deferred sales charge): Charge a commission on redemption (sale) of the fund. The percentage they charge will be high in year-1 but will decrease the longer the fund is held. Once the fund is held for a certain period of time (normally 6 or 7 years) the back end load is reduced to zero. A back end load fee schedule may look something like this\*:

Withdrawal in first year:	7% back end load fee
Withdrawal in second year:	6% back end load fee
Withdrawal in third year:	5% back end load fee
Withdrawal in fourth year:	4% back end load fee
Withdrawal in fifth year:	3% back end load fee
Withdrawal in sixth year:	2% back end load fee
Withdrawal in seventh year:	1% back end load fee
Withdrawal in eighth year (or later):	0% back end load fee

*\*For illustration purposes only*

**Trailer fee (also known as a service fee):** This fee is charged to the unit holders and is paid to the salesperson for the ongoing advice they provide. Once you sell an investor a fund, your job is not done. You must meet with them regularly to ensure that their needs have not changed.

**Exam Tip!** You must know how each fee is collected!

- Management fee: Deducted from the assets of the fund.
- Trailer fee: Paid by the fund company to the salesperson.
- Front-end load: Added to the sales price.
- Back end load: Deducted from the redemption proceeds.

Now that we have given you a basic understanding of what a mutual fund is, we can begin to talk about your new industry!

**Thank you for your interest in SeeWhy Financial Learning. We sincerely hope that you will allow us to be a part of your upcoming exam success!**

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