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https://blog.en.erste-am.com/what-types-of-funds-are-there/

# What types of funds are there?

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Actively managed funds and ETFs – what is the difference?

Behind an actively managed fund there are always fund managers who influence the composition of the fund and actively look after the weighting of individual securities. Actively managed funds can therefore react to different market phases and are realigned by the fund managers if necessary. They keep an eye on the development of the securities contained in the fund and can react quickly if necessary – but only within the legal framework of the respective fund.

In contrast to actively managed funds, ETFs are exchange-traded funds that usually track an index, such as the DAX, or market segments of an index. The shares are composed in the same way as they are contained in the original index. The ETF thus follows the price fluctuations of the shares in the entire index; individual adjustments and corrections of the individual stocks contained are not provided for. Changes in the fund composition only take place when the respective index has been adjusted. As a rule, only a small management fee has to be expected with an ETF. However, the range between the buying and selling price of an ETF should not be ignored. This so-called spread can vary in size depending on the ETF and can also differ from the underlying index. The size of the spread can also vary from trading venue to trading venue and increase due to volatile trading, for example.

Whether actively managed funds or ETFs, there are no guarantees either way. As an investor, you have to consider the possible risk of a capital loss in any case.

What characterises active fund management and what do fund managers do?

### Selection of securities

The key success factor of actively managed funds is the selection of securities using an established selection process. Active fund managers select individual stocks in a certain market segment – for example European stocks – using a previously defined strategy. If a share appears to the fund management to be undervalued in relation to similar shares or the market as a whole and if it fits the orientation of the fund, there is potential for it to be included in the portfolio. If the share price rises disproportionately, fund managers can also sell the share again.

#### Dividing securities (allocation)

Active fund managers act with an eye to the future and can quickly adjust the weighting of the respective category of securities if market conditions change. The composition of individual securities is therefore dynamic and can change over time. If securities prove to be particularly stable, the allocation usually remains the same – values with persuasive power can therefore also be included in funds for a long time.

### Price-conscious buying and selling of securities

Frequent changes in the composition of securities in the portfolio generate costs that must first be earned back through the performance of the fund. Consequently, individual securities are selected very carefully in order to reduce trading costs.

The portfolio invested in the fund is also acquired at fixed closing prices on the stock exchanges.

Due to the active fund management, actively managed funds tend to have a higher management fee. A transaction fee is payable on the purchase of fund units, but only in exceptional cases on the sale.

Once the first step has been taken and the decision to invest in a fund has been strengthened, the next question is: What is included in which type of fund?

### What are asset classes? In which securities does a fund invest?

To get an overview of the different types of funds, it is helpful to look at the so-called asset classes. These are the different types of securities in which a fund invests.

In an equity fund, investors invest indirectly in a large number of individual stocks that are selected by professionals. This broad diversification reduces the risk of individual stocks. However, one should be aware that equity funds in particular can be subject to large fluctuations in value.

Bond funds invest their assets in variable or fixed-interest securities. The bonds are issued by so-called “issuers”. This is a legal entity that issues securities on the money or capital markets in order to raise capital in this way. These securities are usually issued with the help of credit institutions. The issuers of bonds are either states, multinational organisations or companies. Bonds are characterised by the fact that they usually have a certain term and regularly pay out a coupon – i.e. interest. The quality of the issuer, i.e. its ability to service the coupons and repay the capital at the end of the term – the redemption – is of great importance.

In a mixed fund, investments are made in different asset classes, for example in bonds and shares. In this case, investors can benefit from the combination of the growth opportunities of equity securities with the returns from fixed-income securities. Those who have little time to keep themselves informed about what is happening on the markets but still want to invest money in the capital market could consider mixed funds as an interesting option – depending on the orientation of the fund, the risk appetite can be lower or higher with mixed funds.

Alternative investments are capital investments that do not belong to the traditional financial products. These include, for example, hedge funds, private equity funds, but also real estate funds. Depending on their orientation, alternative investments can have a high risk.

### Can I also invest only in a specific sector or country?

For those who prefer a specific sector or country, theme funds offer the opportunity to invest in a more targeted manner. Equity funds can be filtered very well according to sectors or themes, such as biotechnology, technology, or ESG.

For both equity and bond funds, it is possible to choose whether only one country – for example the USA – is desired as an investment region, or whether the fund should be invested internationally.

### A sustainable investment is important to me – what options do I have?

Regardless of the asset class, it is possible to select funds according to their sustainable strategy. This is where the buzzword “ESG” comes into play, which is currently on everyone’s lips. Behind this abbreviation are three core topics of sustainable investment, which also form the focus of our sustainable funds: Environment, Social and Governance.

Erste Asset Management covers a wide range of sustainable investments and differentiates between

- Impact funds (Article 9, Disclosure Regulation),
- Responsible funds (Art. 8) and
- Integration funds (Art. 8).

All retail funds of Erste AM are subject to the guidelines on ethical minimum standards, which include the exclusion of controversial weapons, the renunciation of food speculation and the renunciation of investments in coal.

Depending on the sustainable strategy, different selection criteria are used. For example, the Responsible Funds follow the best-in-class approach. Here, those companies are selected that have the highest ESG standards in a sector comparison – naturally taking into account economic key figures and other exclusion criteria.

All those who want to achieve a direct benefit with their sustainable investment should take a closer look at impact funds. These funds aim not only to generate a financial return, but also to have a measurable, positive impact on the environment or society.

### What else is important to consider?

Apart from asset classes and sustainability criteria, there are other factors that are important when choosing a fund:

Most funds have a distributing or an accumulating variant. The distributing tranche distributes an amount every year on a certain date, which is determined anew each year by the investment company. This amount is then credited to the investor’s account. With the accumulating tranche, on the other hand, only the tax incurred is distributed, the rest remains in the fund.

The income from a fund investment is subject to tax. If the fund is a domestic fund held in a custody account at a domestic bank, these taxes are automatically paid. It should be noted that this information is only valid for private clients in Austria.

### Conclusion

The choice of a fund should be well considered – but it does not have to be a big hurdle. Features such as asset classes, sectors and countries make it possible to narrow down the choice of funds.

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