Standard Life

Risk and market-related funds

It's important that you understand the different types of investment funds offered under your group savings and retirement program, and the risks associated with each, in order to select and monitor your investment mix.

This information sheet provides you with more insight on market-related funds and the types of risk they may entail.

Investing in market-related funds

When you invest in a market-related fund, your money is pooled with the money of others who invest in the fund. Market-related funds invest in a variety of securities (e.g., Treasury bills, bonds, company shares), depending on the specific investment objectives of each fund. The decision to buy and sell various securities is made by professional investment managers, also known as fund managers. The fund managers use your contributions and those of the other investors in order to purchase a number of securities for the fund. The fund's performance depends on the combined overall performance of the different securities it holds.

Your participation in the fund is represented by units. For each contribution you make, your account is credited with units (or fractions of units) based on the unit price at the time you invest. The Unit Value of the fund changes in accordance with the value of the securities it contains and the fund's income, expenses and Investment Management Fees.

Because of this, your investments in market-related funds are not guaranteed. That means that the value of your investments may, by the time you redeem your units, be more or less than what they were when you purchased them.

Market-related funds overview

Market-related funds can be broken down into three investment categories: Fixed income funds, Balanced funds and Equity funds.

Fixed income funds

Fixed income funds invest primarily in the debt (Treasury bills, bonds or short-term notes) of corporations or governments, and are typically broken down into money-market funds and bond funds. Mortgage funds are also classified as fixed income funds.

Balanced funds

Balanced funds, also known as diversified funds, invest in a mix of company shares, bonds and short-term investments. The percentage held in each type of investment is adjusted by the fund manager in accordance with the objective of the fund and depending on the market conditions.

A balanced fund will typically perform better than an equity fund when stock values are falling, but less when they are rising. Balanced funds are generally found in the middle of the risk/return scale.

Equity funds

Equity funds invest primarily in the ownership (stock) of publicly traded companies in Canada, the US, and abroad. Equity funds are characterized by the size, location and the nature of the companies the fund invests in.

Historically, equity funds have offered investors better returns over the long term than other investment categories, but have also experienced more fluctuations in value, and are, therefore, considered riskier.

Understanding risk

Each market-related fund bears a number of risks, depending on the securities it holds and its investment objectives and strategies. While some funds will, by nature, carry a larger number of investment risks, that doesn't necessarily mean those funds are riskier. Diversified funds for example, are considered safer investments than equity funds.

Risks can be managed so as to offset each other. The fund manager's role is to use a number of risk management strategies (such as diversification), so that the overall level of risk of the fund is in line with the fund's objectives and expected level of return.

The risks associated with market-related funds

The following describes the various investment risks that may be present in market-related funds, according to their type.

We strongly encourage you to use this information, in conjunction with the fund summary sheets provided in the Rates and Closing Values section of the VIP Room website, when making your investment selection.

1. Market risk

Fixed income – Balanced – Equity

The unit value of a fund will fluctuate daily with changes in the market value of the fund's investments. Such changes in market value may occur as the result of various factors, including general economic and market conditions, the level of interest rates, specific industry and company factors, as well as political and international developments.

2. Interest rate risk

Fixed income – Balanced – Equity

An increase in interest rates may negatively impact the price of any asset within a particular fund, thus reducing the overall return of the fund.

3. Inflation risk

Fixed income – Balanced – Equity

The overall fund performance may be negatively affected by the impact of inflation on interest rates, which, in turn, makes any assets within a fund less attractive from a price perspective.

4. Currency exchange risk

Balanced* – Equity*

The currency of a country in which a fund invests may decline in value relative to the Canadian dollar, adversely affecting the returns of any foreign securities held in the fund and the total return of the fund.

5. Liquidity risk

Balanced – Equity

Liquidity refers to an investor's ability to sell an asset and convert it to cash quickly. Difficulty in selling securities may result in a loss and/or in costly delays. The equity of smaller companies, mortgages and some foreign investments are examples of assets that are somewhat less liquid.

6. Credit risk

Fixed income – Balanced – Equity

Credit risk refers to the risk that the government or company issuing a fixed income security will be unable to make interest payments or pay back the original investment. Credit risk is lowest among issuers with solid financial conditions and good credit ratings. Debt issues by the Government of Canada have the highest credit ratings in Canada and, therefore, the lowest credit risk.

7. Foreign market risk

Fixed income* – Balanced* – Equity*

Investing in foreign markets involves greater diversification and potentially higher returns, but encompasses greater uncertainty, due to currency fluctuations and different economic, regulatory, political environments and borrowing/debt repayment conditions.

8. Income trust risk

Fixed income* – Balanced* – Equity*

Some funds may invest in income trusts, such as real estate investment trusts or royalty trusts. In some provinces, an investor in a trust may be held liable for certain obligations and claims of the trust. To the extent that the assets of the income trust do not satisfy the claim, there is a risk that the investors can be held liable for the obligations of the income trust.

9. Derivative risk

Fixed income – Balanced – Equity

Derivatives have their own special risks. Here are some of the common risks:

- Using derivatives for hedging may not always work as intended.
- There is no guarantee that a fund can close out its position in a derivative contract when it wants to, due to exchange-imposed trading limits.
- Derivatives traded on foreign markets may be harder to trade and have higher credit risks than derivatives traded in North America.
- The other party to a derivative contract may not be able to live up to its agreement to complete the transaction.

10. Performance tracking risk

Fixed income* – Balanced *– Equity*

Many of the market-related funds offered to retirement programs by Standard Life are funds that invest in units of another fund (the underlying fund). The performance of these funds, relative to the performance of the underlying fund, may be impacted by large transactions, relative to the fund's size.

11. Concentration risk

Equity*

Some retirement programs include a market-related fund that invests only in the stock of the program's sponsor. Greater risk is associated with a single-stock type of fund, which makes it important to combine this investment with investments in other funds to achieve adequate diversification.

* Where applicable

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