FINANCIAL LITERACY
FOR YOUTHS

Unit Trust Funds

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Unit trust funds, these three words may sound familiar to you, or might be perceived as words from the German language. If this is the first time you're reading about these three words, do not get too panicked. You are definitely not alone in this country.

So, what are unit trust funds?

A unit trust fund is an investment vehicle where a pool of investors' money is gathered to be invested in various securities. The gathered funds are separated into different pools and invested according to the risk appetite or different groups of investors. The fund will be managed by a professional fund manager who will invest the money in various financial assets, such as stocks, bonds, and other financial instruments deemed suitable by the fund manager. Investors only supply cash according to their will to the unit trust and the firm will manage the money and grow it following their outlined strategies and guidelines.

When did It Began?

Actually, unit trust funds have been in Malaysia for almost 60 years, which is in fact older than most of the Gen X residents in Malaysia. We are blessed to be introduced with unit trust funds earlier than our neighbours. The first unit trust company in Malaysia, the Malayan Unit Trust Ltd. was established in 1959.

However, it was not until the 1970s unit trusts funds started garnering renown from Malaysian investors. 10 years ahead, it saw a rapid growth through banks and other institutions, such as Permodalan Nasional Berhad through its subsidiary, Amanah Saham Nasional (ASN). Ever since, the industry has grown relatively well and the government has enacted laws to regulate the industry and protect investors interests. Today, there are numerous unit trust funds serving as a branch of service provided by numerous financial institutions such as major banks, insurance service providers and investment vehicles.

Why Unit Trust Funds?

Unit trust funds can be extremely convenient for those who are worried about their financial future but do not have the time and expertise to dedicate themselves to the field of investment.

Indeed, the field of finance is getting extremely complex in the 21st century and understanding different type of investments can be demeaning and time consuming. The dedication and time required to understand the art of investment is high and not every person can manage such a large commitment, taking other responsibilities into consideration. For these super busy people who hope to earn some extra income, unit trust funds exist as a solution. Investors can be laid assured and let professionals that are well-trained in the field of investment and finance to manage their money.

Other than that, there are several reasons to invest in a unit trust, especially for non-professionals and those lacking knowledge in investment:

- **Can be affordable for most people**

In Malaysia, one could easily open a unit trust account with any unit trust fund provider with a minimum amount of RM100. Yes, RM100! This allows most people including students and the middle class to open an account and invest their money into the unit trust. Other than that, management fees for unit trust funds are lower than transaction fees for retail investors that are involved directly with financial assets such as stocks in Bursa Malaysia. This is because unit trust funds are involved in large transactions, which allow them to pay less in transaction fees due to the economies of scale compared to retail investors.

- **Diversified Portfolio**

Unit trusts invest in a variety of assets classes ranging from financial assets such as stocks, bonds, and derivatives to real, tangible assets like real estate. Because of this, investors can obtain indirect access to financial markets that most retail investors will not have access to, such as Malaysian Government Securities market due to the nature of transactions involved in these markets. Investors investing their money in unit trusts will find their investments immediately diversified following the package of unit trust offered and the level of risk that they are willing to take. A diversified portfolio reduces the risk involved in any investment thus benefiting investors.

- **High Liquidity**

Unit trust funds are very liquid, which means that any deposits in any unit trust fund can be converted into cash rather quickly. This allows investors to cash out their money whenever they require the money, be it emergency situations or other situations. Because of that, unit trusts are perceived as a type of safer investment.

- **Well-regulated**

Unit trusts are regulated by the government under the Capital Markets and Services Act 2007. Under this Act, the Securities Commission of Malaysia is given the responsibility to provide guidelines on unit trust funds which has been revised multiple times over the span of 5 years (2009, 2010 and 2014). The Securities Commission also oversees and ensures that unit trusts obey these guidelines to protect investors' interests.

Choosing a unit trust fund

Alright, enough of convincing, you might have this question popped up in your mind by now: "How do I choose and invest into a good unit trust?".

Great question! Before choosing a unit trust fund, one should realise the risks involved investing into unit trusts. **Remember, there is NO such thing as a risk-free investment or an investment with guaranteed returns, and any investments that has similar nature as one of the two types stated above is HIGHLY LIKELY to be scams or ponzi schemes.**

So, what are the risks involved?

- **Risks from management**

A poorly managed fund will not give satisfactory returns or even cause the investment to lose capital. This can be prevented by looking at the background of the fund managers to ensure that these managers are competent enough to maximise gains and prevent capital loss in their investments. Fortunately, majority of unit trust funds in Malaysia have stellar performances. However, it is best to keep in mind that past performance is never an indicator of future performance and should not be the sole criteria to be considered when selecting a fund.

- **Risks from stock market**

Unit trusts will have portfolios with exposure to the stock market. Thus, fluctuations in the stock market will affect the value of investment owned by the unit trusts. Investors need to be aware about this and also the type of stocks and portfolio exposure when deciding to invest in a unit trust. Normally, investors can demand to have a view of different packages of unit trusts with different portfolios and choose the one which satisfies the risk appetite. Knowing more about your investment can help to mitigate risks, and in this case, risks involved with stock market fluctuations.

- **Interest rate risk**

Unit trusts also invest in bonds and financial derivatives that may be affected by interest rates. Interest rate is a powerful tool that can determine the fluctuation in the financial markets in general. Thus, knowing about the risks carried by interest rates may allow investors to make better decisions in choosing a fund.

- **Inflation risk**

Inflation is something that must be considered while choosing a unit trust fund. A fund that provides lower returns than the rate of inflation in a particular year will cause a reduction in value of the investment because the purchasing power of the fund decreases due to inflation.

For example, an investor buys a fund worth RM10,000 with a unit trust A. One year later, the unit trust declared a growth of 3% in the investment. However, the inflation rate of the year was 4%. While your money has grown by 3%, taking into consideration inflation, your purchasing power has decreased by 1%. This actually means that in reality, your fund has decreased in value by 1% due to inflation!

Because of that, investors must be aware of the risks posed by inflation when deciding in a unit trust to invest.

- **Shariah-status reclassification risk**

Shariah-status reclassification risk is mainly for Muslim investors and investors interested to invest in Shariah-compliant unit trust funds. Securities Commission will evaluate unit trust funds every two years and decide if these unit trust funds are Shariah-compliant. Thus, those opting Shariah-compliant funds may have to immediately change unit trust if their current unit trust is declared to be non-Shariah compliant per Securities Commission standard.

After considering these risks, then investors should decide on the unit trust fund of their choice based on their risk appetite.

Conclusion

In short, unit trust funds are useful for investors without the advanced knowledge and time to dedicate themselves to invest their money by themselves. It is also useful is an investor wishes to diversify their portfolio. Hence, everyone should know about unit trusts, how they function, and choose the best funds based on the risks associated with them..

Be a wise investor, and be smart in doing your financial decisions!

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