Collective investment schemes

What are collective investment schemes?
Collective investment schemes are pools of assets supplied by investors to be jointly invested on their account. They make broadly diversified investments possible with a small amount of invested capital.
Collective investment schemes come in many different forms and are extensively regulated in Switzerland. In particular, they are subject to approval and supervision by the Swiss Financial Market Supervisory Authority FINMA. The main form of collective investment scheme is the contractual investment fund. Investors in Switzerland can choose from a wide range of foreign funds in addition to Swiss-domiciled ones. Collective investment schemes may adopt various strategies: money market, equities, bonds, asset allocation, real estate, commodities or alternative investments. The legal documents constituting a fund – the fund regulations, articles of association or fund contract – describe the investments it can make

What risks are associated with collective investment schemes?
Funds are subject to the same market, volatility, country, currency, liquidity and issuer risks as the investments they make. The extent of specific risks depends on their investment restrictions, risk diversification and use of investment techniques and derivatives. The legal documents constituting a fund, as well as its prospectus and (where applicable) key information document, describe its risk profile in detail.

Market risk
The risk of price fluctuations within a given period due to factors impacting a specific market. Volatility is the generally accepted measure of market risk.

Currency risk
Risk of exchange-rate fluctuations if the reference currency is not the currency of the financial instrument.

Liquidity risk
The risk that an investor will not always be able to sell an investment at an appropriate price.

Issuer risk
Risk of the issuer of the financial instrument becoming insolvent.

Swiss collective investment schemes
Swiss collective investment schemes are governed by the Collective Investment Schemes Act (CISA), which recognises the following categories of collective investment scheme:

Contractual and company-law collective investment schemes
The main form of collective investment scheme in Switzerland is the contractual investment fund. Other forms are investment companies with variable capital (SICAVs), investment companies with fixed capital (SICAFs) and limited partnerships for collective investment.
With a contractual investment fund, the relationships between the investors, the fund management company and the custodian bank are set out in a fund contract. The fund management company manages the fund on behalf of the investors. It makes the investment decisions, keeps the accounts and performs all administrative tasks. The custodian bank holds the fund's assets in custody. It takes care of payments and is responsible for issuing and redeeming fund units.
Contractual investment funds are open-ended funds, i.e. investors have the right to terminate the contractual relationship at any time by redeeming their fund units at the net asset value (NAV). New investors can also buy into the fund. Fund management companies, SICAVs, SICAFs and limited partnerships are comprehensively regulated, require authorisation from FINMA and are supervised by FINMA. The assets of a contractual collective investment scheme under Swiss law are segregated (see Glossary) in favour of investors if the fund management company goes bankrupt. In the event that a bank or securities dealer acting as custodian goes bankrupt, the owners of custody account assets (e.g. movable objects and securities) are entitled to have those assets segregated from other assets (see Art. 37d BA, Art. 17 FISA, Art. 35 CISA). This has the effect of excluding the assets from the bank or securities dealer's bankruptcy assets and ensuring they remain with the account holder. Such segregation is not required for SICAVs, SICAFs and limited partnerships as they are legally separate companies.

Cornèr Banca SA // Via Canova 16 // 6901 Lugano_Switzerland
Tel. +41 91 800 51 11 // corner.ch // info@corner.ch

Open-ended collective investment schemes
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Closed-ended collective investment schemes
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Securities funds and other funds for traditional and non-traditional investments
Open-ended collective investment schemes under Swiss law are divided into the following categories according to their investment guidelines: securities funds, other funds for traditional investments, other funds for alternative investments (see Glossary) and real estate funds. Alternative investments is an instrument that has little or no correlation with the conventional financial markets, such as equities and bonds. Examples include hedge funds, private equity and commodities. Securities funds invest in securities or rights issued on a large scale and traded on an exchange or another regulated market that is open to the public. They are intended for investments in liquid financial instruments and can only invest in other financial instruments to a limited extent. Other funds for traditional investments and for alternative investments are subject to less strict investment rules than securities funds. They also have more scope than securities funds as regards their use of investment techniques and derivatives

Foreign collective investment schemes
The legal structure and investment rules of foreign investment funds are determined by the laws that apply in their respective countries. Funds that comply with the EU Directive on Undertakings for Collective Investment in Transferable Securities (UCITS) are especially common. The Directive sets out requirements in terms of organisation, types of instrument used and liquidity that funds must meet in order to be sold to a broad spectrum of investors.

Investment strategies of collective investment schemes
The investment opportunities open to collective investment schemes vary according to their legal form and category. The investment strategy set out in a collective investment scheme's legal documentation (fund regulations or articles of association, depending on the legal form) defines the investments it can make. Collective investment schemes' strategies are geared first and foremost to risk diversification. Below are some examples of possible investment strategies.

Money market funds
Money market funds invest in short-term, fixed-income instruments and are suitable for short-term investment purposes.

Equity funds
Equity funds invest mainly in shares. They are normally categorised by geographical focus (country-specific, regional or global), sector or theme (e.g. banks, pharmaceuticals, technology) or company size (small, medium and large caps). Equity funds have high potential for returns over the long term but also a high volatility risk. They are therefore suited to investors with a long-term focus who wish to profit from the economic growth of one or more countries or sectors.

Fondi obbligazionari
Bond funds Bond funds invest mainly in bonds with fixed or variable coupons, convertible bonds and warrant bonds. They are categorised primarily by currency, credit rating and length of term. They are suited to investors with a medium- to long-term focus seeking more regular income from coupon payments.

Asset allocation funds
Asset allocation funds invest in a range of different asset classes, e.g. shares, bonds and real estate. Also known as portfolio, mixed or strategy funds, they pursue specific strategies. They offer a standardised form of asset management tailored to investors' individual objectives and risk tolerance, allowing them to diversify risks in line with their risk profile for a relatively small invested capital.

Actively managed investment funds
With actively managed investment funds, the fund manager chooses the mix of asset classes and individual securities in accordance with specific criteria, continually monitors the portfolio and adjusts it as required. The fund's performance is measured against a reference index known as the benchmark, and the fund manager attempts to add value for investors by constructing a portfolio that outperforms the benchmark.

Passively managed investment funds and ETFs
Passively managed investment funds, also called index funds, track a market index, which significantly reduces management costs. Their investment decisions are essentially determined by changes in the index. Passively managed investment funds thus offer a simple and cost-effective way of ensuring broad diversification. Exchange-traded funds (ETFs) normally track an index, e.g. a share, bond, money market, real estate, hedge fund, currency or commodity index. They offer the advantage of being easy to trade

Funds of funds and multi-manager funds
Investment funds that invest in other funds (target funds) rather than individual securities are known as funds of funds. The target funds can invest in a wide range of securities. Multi-manager funds spread their investments among a number of fund managers covering different investment styles, markets and financial instruments. Investors can achieve a higher level of risk diversification by investing in funds of funds and multi-manager funds, but the costs are generally higher due to the costs generated by the various underlying funds. Investors should also bear in mind that certain categories of funds of funds and multi-manager funds domiciled in countries with strict legislation on collective investment schemes may follow strategies that are to some extent similar to those of offshore and hedge funds.

DISCLAIMER

This information sheet contains an extract from the brochure "Risks Involved in Trading Financial Instruments" published by the Swiss Bankers Association (SBA), the complete version of which can be consulted at www.swissbanking.org or on the Bank's website (www.corner.ch).

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Before making any investment decision, we invite you to consult a financial advisor and to examine carefully all documents and information available for each financial instrument (prospectus, basic information sheet, term sheet, etc.).

Cornèr Banca SA // Via Canova 16 // 6901 Lugano_Switzerland
Tel. +41 91 800 51 11 // corner.ch // info@corner.ch