INVEST SMART

Mutual Funds 101

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(NAPSA)—Picking individual stocks is tricky; buying individual bonds can be expensive. That's the reason mutual funds were introduced: To allow the small investor to participate in the stock and bond market for just a small initial investment.

A mutual fund pools the money of many investors and uses it to invest in stocks, bonds, money market instruments and other types of securities. Put together by an investment company, mutual funds are managed by a professional who buys and sells securities in an attempt to accomplish the fund's pre-established objective (i.e. long term vs. immediate investment returns).

Think of mutual funds like pizza. If you cut the pizza, you get slices. Cut the mutual fund and you get shares. If the pizza has pepperoni and pineapples, the slice will have a portion of those toppings. Similarly, each share gets a portion of the mutual fund's gains, losses and income, and each share pays a portion of the fund's expenses. For example, if the fund is trading at $10 a share, your $1,000 investment will buy 100 shares. The share price of 410 is called the net asset value, or NAV.

Every business day, the investment company calculates the value of all the securities in the portfolio. It deducts expenses, which include management fees, administrative costs, advertising expenses and brokerage fees. What's left is divided by the number of shares in the pizza to come up with the value of a single share, or the NAV.

Now that you understand how mutual funds work, here's why investors like them: Just like pizza appeals to both meat and veggie eaters, mutual funds appeal to both stock and bond investors. Why? Because it enables them to participate in either market—or both—for just a small initial investment.

Building a good mutual fund portfolio is a little like making a pizza. The right mix of ingredients can mean delightful results.

With more than 8,000 different mutual funds, how do you determine which is right for you? Simply identify your investment objective and match it with the most appropriate fund objective.

For most investors who are just getting started and feel intimidated about picking individual securities, mutual funds provide the best solution; professional management, instant diversification and convenience.

Mutual funds also offer flexibility and variety. You can pick from conservative, blue-chip stock funds, funds that aim to provide income with modest growth or those that take big risks in the search for returns. You can even buy balanced funds, or those that combine stocks and bonds in the same fund.

Exactly how much money you make or lose in a mutual fund can change daily, as it all depends on how many shares you own and how well your mix of investments performs.

To find out which funds are right for you, visit the investing section of CNBC on MSN Money (http://money.msn.com), or check out the comprehensive personal finance management software, Microsoft Money, which helps you track investments and stay abreast of market-moving news.