The purpose of swing pricing in pooled investment funds is to provide protection to current fund shareholders against the negative dilution impact from transaction/trading costs occurring when a fund buys or sells securities as a result of external cash flows driven by fund shareholders (subscriptions and redemptions). This is achieved by transferring the estimated impact arising from transaction costs to those shareholders that subscribe or redeem fund shares. In principle, the fund's tradable NAV is adjusted with a so-called "swing factor" so that the shareholders who subscribe buy shares at the swung NAV that is higher than the valuation or unswung NAV. Shareholders who redeem sell shares at the swung NAV that is lower than the valuation or unswung NAV.

There are various approaches to swing pricing that depend on specific parameters, for example:

- Dual pricing versus single pricing: Dual-priced funds calculate one price for subscribers and another price for redeemers, while single-priced funds calculate one single NAV per share that is used for all capital activity (both subscriptions and redemptions).
- Full swing versus partial swing:
    - For full swing funds, the NAV is adjusted each time there is capital activity. The direction of the swing is determined by the net capital activity of the day (i.e., net inflow or outflow).
    - For partial swing funds, the NAV is swung only on those days when a predetermined net capital activity threshold (the swing threshold) is exceeded. As with full swing, the direction of the swing is determined by the net capital activity of the day (i.e., net inflow or outflow). Partial swing is also referred to as semi-swing pricing.

In all cases, the size of the swing factor is determined by the size and direction of the capital flows. Typically, funds that apply swing pricing calculate two types of NAV per share – the "unswung" or "valuation" NAV and the "swung" NAV. Dual-priced funds will have three prices: the valuation NAV, the swung NAV for subscriptions, and the swung NAV for redemptions. Single-priced funds will have two prices: the valuation NAV and the swung NAV.

Performance Calculation for Pooled Funds that Apply Swing Pricing

Pooled funds may calculate their performance either on the basis of NAV per share or on the basis of the total fund portfolio taking into consideration external cash flows.

Those pooled funds that calculate their performance on the basis of the NAV per share and apply swing pricing should consider the following advantages and disadvantages associated with using the swung NAV or the unswung NAV for performance calculation purposes:

Advantages of Swung NAV

- Best representation of investor return. More appropriate for investment performance reporting to current investors because the return of the fund is based on traded NAV

Disadvantages of Swung NAV

- Introduces additional volatility and tracking error and reduces comparability against benchmark (benchmark performance does not include swing factor impact)
- Reduces comparability against other investment managers as swing factors may be subjective and vary from manager to manager

Advantages of Unswung NAV

- Best representation of manager return. Better comparability among investment managers. More appropriate for prospective investors
- Return is more comparable to portfolios that are not pooled funds (i.e., segregated portfolios) included in the same composite
- Better comparability against benchmark (benchmark performance does not include swing factor impact)
- More appropriate as the basis for performance fees

Disadvantages of Unswung NAV

- Unswung NAV is not a traded NAV that is available to investors for subscriptions/redemptions – performance does not fully correspond to the individual investor's return
- Unswung NAV may not be published or readily available

For GIPS compliance purposes, firms are allowed to use either the swung or unswung NAV as the basis of the fund's performance calculation. Due to the advantages described above, firms are recommended to use the unswung NAV. Firms must include policies and procedures with respect to the use of swing pricing in calculation and valuation policies and procedures and apply them consistently on a composite-specific or fund-specific basis. Firms must disclose that policies for valuing portfolios, calculating performance, and preparing GIPS Reports are available upon request. Some countries may have regulatory guidance in place with respect to the use of swing pricing for fund performance calculation purposes. Firms are reminded that they must comply with all applicable laws and regulations regarding the calculation and presentation of performance.