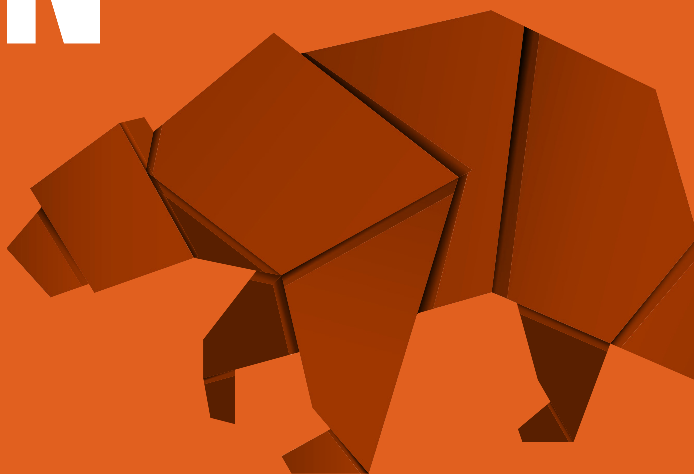
BetaShares
Exchange Traded Funds

DEBUNKING THE MOST COMMON MYTHS ABOUT ETFS



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ABOUT US

BetaShares is a leading manager of ETFs and other Funds that are traded on the Australian Securities Exchange ('ASX'). Our aim is to provide intelligent investment solutions, which help Australian investors meet their financial objectives.

With a broad range of products now trading on the ASX, our range of Funds is one of the largest and most diverse available in the market. We offer investors simple to use and cost-effective access to equities, cash, currencies, commodities and alternative strategies.

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DEBUNKING THE MOST COMMON MYTHS ABOUT ETFS

BetaShares has compiled a list of the top nine most common misconceptions about ETFs, and reveals the reality behind the myths.

MYTH #1:
ETFS ARE A “FAD”

The argument that ETFs are in any way a temporary or fleeting investment option is just not supported by the facts. ETFs have been around globally since 1990, in Australia since 2001 and the good news is that they are here to stay!

To put some numbers to this, the amount invested in ETFs is now over US$6.1 trillion globally, and typically make up 1 out of every 3 trades on the largest stock market in the world, the New York Stock Exchange (NYSE).

MYTH #2:
ETFS ARE RISKIER THAN TRADITIONAL MANAGED FUNDS

Many investors find themselves questioning if they would be better off investing in an ETF or a traditional managed fund, and which type of fund will best serve their portfolio.

But investors should remember that both fund types have more similarities than differences. Instead of seeing ETFs as riskier, investors should think of traditional index funds and ETFs as the same basic product, just in different forms – one is trading on a stock exchange like a share, the other is bought via application forms.

MYTH #3:

ETFS CAN'T OUTPERFORM THE MARKET

ETFs are generally considered "passive" funds, given the way that they are structured to track a benchmark index. This leads many to dismiss them as being incapable of outperforming the market, but this isn't true.
An investment strategy implemented via ETFs can indeed be structured to give you an opportunity to generate returns that outperform the market.

For example, by adding ETFs that give your portfolio access to asset classes that you otherwise would not have had, or using ETFs to 'overweight' a portfolio to one particular sector, you can combine with broad market ETFs with a view to outperforming what would be capable with a broad market exposure alone.

It's all about how you are using ETFs within your portfolio. Put simply, a portfolio comprising ETFs can offer an investor the potential to outperform the market.

MYTH #4:

ALL ETFS ARE EQUAL

ETFs are now offered over virtually every asset class, region, country or strategy that you can think of. In this way, viewing all ETFs as the same would be equivalent to viewing all managed funds or shares as the same.
ETFs really need to be considered as an investment structure, not an asset class.

To put it even more starkly, is a Gold ETF the same as an ETF that tracks the performance of the Japanese sharemarket – of course not!

MYTH #5:
ETFS ARE ILLIQUID

Liquidity is one of the most common misconceptions surrounding ETFs, but luckily it can be easily explained.

As ETFs are traded on the exchange, just like a stock, this means that there are 'on-screen' volumes that can be viewed – this sometimes causes confusion around liquidity.

ETFs are 'open ended' structures which means that if there is more demand for the ETF than there are currently available units, new units can be created, or alternatively redeemed when demand is lower. This means that when it comes to trading, the volumes that are shown on the screen are not a meaningful reflection of the ETF's true liquidity.

The actual liquidity of an ETF reflects the liquidity of the underlying stocks (or other assets) that form the ETF. As long as the underlying asset is liquid, the ETF should be considered liquid.

MYTH #6:
WITH ETFS YOU DON'T OWN ANYTHING

This myth seems to persists, but it's a load of nonsense! Let's take the example of an ETF which aims to track an index of Australian shares. In order to provide that exposure to an investor, the ETF manager generally buys the shares in the proportions in which they make up the index, which are then held by the appointed custodian for the benefit of the ETF investors. What that means is that, as an investor in an ETF, every unit you hold gives you an equal ownership interest in the ETF's assets as a whole – in this example, the shares which the ETF manager has bought. Incidentally, the nature of your ownership interest in an ETF is the same as for a traditional managed fund.

MYTH #7:

ETFS ARE TAX INEFFICIENT

The amount of trading inside an ETF or managed fund is typically what determines its tax-efficiency. As the underlying holdings in ETFs typically are required to be traded less frequently than actively managed funds, for example, they are generally considered more tax efficient than traditional managed funds.
ETFs generally realise fewer capital gains than actively managed funds, and this is due to the low turnover nature of passively managed funds. Thus, the tax efficiency of ETFs can actually be relatively high.

MYTH #8:

ETFS ARE INEFFICIENT

There's a claim often made about ETFs that they drive up stock prices regardless of their fundamental value, and that this introduces volatility into the market.

There might be something in this argument if ETFs accounted for enough of the stock market to impact it across the board. For example, the total value of the ASX stock market hovers somewhere around $1.85 trillion. ETFs, for all their growth, account for around $35 billion of that stock market. So it sits at around 2% of the overall value of the stock market.

Even if ETFs behaved in such a way that could create a "bubble" like environment like the ASX, at 2% of the total market, all the ETFs combined wouldn't be able to move the needle on the ASX enough to impact it broadly.

Perhaps even more importantly though, the only thing that is responsible for market volatility is the behaviour of investors themselves. So whether they are expressing their views via ETFs or direct shares or managed funds it is not the structure itself that is driving that behaviour.

MYTH #9:

ETFS DISTORT THE MARKET

A myth often written about ETFs is that they distort the market by buying shares that active fund managers wouldn't necessarily buy.

But, if you were to compare the stocks held by the largest ETFs in the world (which are typically broadly diversified equities products) with the portfolios that the active managers curate, you'd notice quite quickly that there's significant crossover. In other words, ETFs and the portfolios that active fund managers construct will, for the most part, contain very similar stocks.

IN SUMMARY

As you can see, there is a lot of misinformation out there about ETFs, how they work, and the impact that they have on the market.

If you have further questions about ETFs, the myths and truths about them, be sure to contact the experts at BetaShares.

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