

MV Capital Management Midweek Market Commentary

Happy Birthday to You, ETPs!

December 20th, 2012

This January the first exchange-traded fund (ETF) in the U.S. – now called the SPDR S&P 500 – will celebrate its 20th anniversary. Exchange-traded products (ETPs), including both exchange-traded funds and exchange-traded notes (ETNs), offer a multitude of benefits to investors including lower fees and direct exposure to a wide range of asset classes from the staple must-haves for any portfolio to the exotic realms of emerging markets currencies and buy-write option strategies. While many investors have already taken up ETFs for their portfolio we expect this trend will continue in the months and years ahead.

Exchange traded products have grown tremendously over the two decades since SPDR's maiden voyage. There are now around 1,436 products in total, comprising \$1.3 trillion in assets. This is still a far cry from the estimated \$10 trillion that is invested in mutual funds. But investors are showing an increasing propensity to do what we at MVCM have been doing some time now – using ETPs are a core component of a prudently diversified asset allocation strategy.

The evidence that has accumulated over time – and to the core feature of our approach to investment management – shows that the most important decision investors can make is around strategic asset allocation, and ETPs serve a valuable role here. For one, you don't have to worry about your fund manager straying from the stated strategy in search of better returns. Style drift, as this is called, is not helpful from an asset allocation standpoint. With ETPs you know what you are getting – large cap value equity, total return bonds or what have you. Lately, ETFs and ETNs have been launched that offer even more specific objectives such as high dividend yields, lower volatility and many alternative investment options, allowing advisors to diversify across a very broad and deep range of asset classes.

Another area where ETPs are likely to grow is in 401(k) plans. New regulations put in place earlier this year require more transparent fee disclosure to retirement plan participants, including the fees related to the plans' investment choices. The generally lower fee structure of ETFs will likely attract more plan sponsors and managers to utilizing these vehicles in greater number going forward.

So let us all wish exchange-traded products a very happy 20th and appreciate the value they have brought to the world of investing. We expect the next two decades will be promising indeed for their continued growth.

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