

Report

Unlocking ETF Trends



ETFGI

BWV

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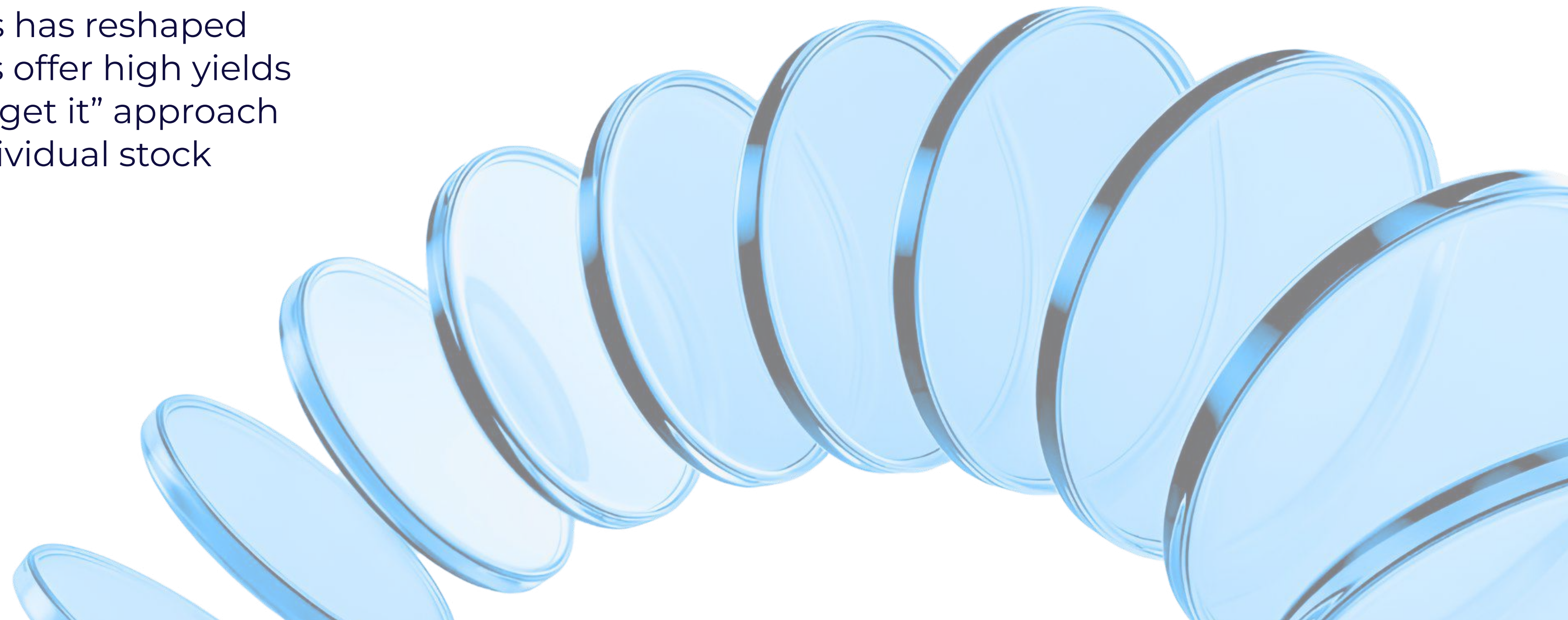
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Introduction

The Exchange-Traded Fund (ETF) industry has transformed the investment landscape, offering unprecedented access and flexibility to investors worldwide. ETFs have become synonymous with simplicity, yet behind their apparent ease lies the potential for significant market impact, particularly on trading volumes and individual stock investments.

The growing dominance of ETFs has reshaped market dynamics. Because ETFs offer high yields and low fees, their “set it and forget it” approach often leads to a reduction in individual stock trading activity.

Understanding this shift is crucial, as ETFs now play a pivotal role in market liquidity and investor behavior. This report will not only help you harness the potential of ETFs but also help you understand the broader implications of these tools and their impact on the overall investment landscape.



The Evolution of ETFs

From Inception to Mainstream Adoption

The ETF industry, though relatively young compared to traditional investment vehicles, has seen huge growth over the past three decades. In this time, ETFs have evolved from a niche product to a mainstream investment option, offering exposure to a wide array of asset classes, sectors, and strategies.

The ETF industry's growth is not just in numbers but also in the diversity of products, catering to a wide range of investment strategies and preferences. Today, there are over 12,321 ETF products listed on 80 exchanges across 63 countries, managed by 752 providers.

History of ETFs

1990

The first ETF was launched in Canada, marking the birth of a new investment vehicle.

1993

The United States introduced its first ETF, the SPDR S&P 500 ETF (SPY), which has since become one of the most traded ETFs globally.

2000

Europe entered the ETF market, with the introduction of LDRS STOXX and EURO

One of the key factors behind the ETF industry's growth is that they level the playing field between large institutions and individual investors. Both institutional and retail investors can access the same ETF products at the same cost.

While mutual funds have been around for a century, ETFs offer several advantages:

- **Trading Flexibility:** ETFs trade like stocks on an exchange, allowing intraday trading and greater liquidity.
- **Cost Efficiency:** Generally lower fees due to passive management and economies of scale.
- **Tax Efficiency:** The unique creation and redemption process minimizes capital gains distributions.
- **Transparency:** Daily disclosure of holdings provides investors with clarity on their investments.

These benefits have led many investors to prefer ETFs over mutual funds, especially as they seek to optimize returns and manage costs.

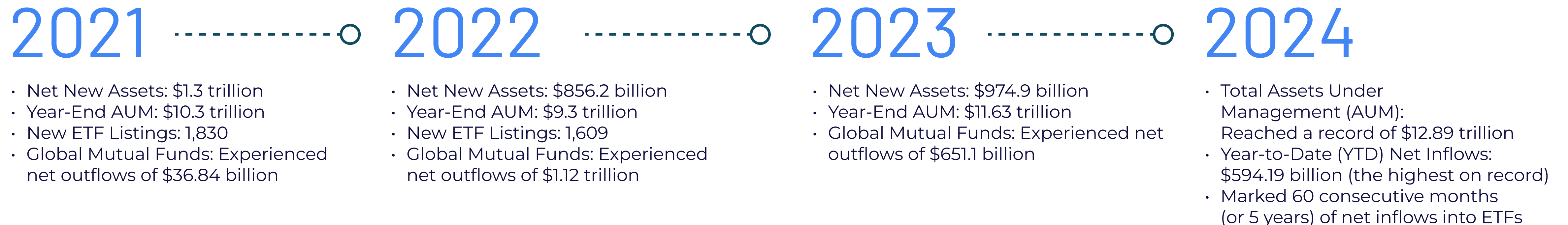


Asset Growth and Market Expansion

One of the most compelling indicators of the ETF industry's strength is its consistent net inflows. For 60 consecutive months, the industry has seen positive net inflows, totaling nearly \$600 billion in just the first five months of 2023. This sustained momentum reflects strong investor confidence in ETFs as reliable and efficient investment vehicles, even during periods of market volatility.

In contrast, mutual funds have experienced net outflows over the same period, signaling a significant shift in investor preference toward ETFs. Factors contributing to this trend include ETFs' typically lower fees, greater transparency, tax efficiency, and the flexibility they offer through intraday trading on exchanges.

ETF Growth



Driving Forces Behind ETF Growth

Institutional Adoption

Institutional investors are increasingly utilizing ETFs for portfolio management, tactical asset allocation, and risk management strategies. The liquidity and transparency of ETFs make them suitable tools for implementing sophisticated investment approaches.

Regulatory Support

Evolving regulatory frameworks in various jurisdictions have enhanced the appeal of ETFs. Improved regulations around disclosure, trading practices, and investor protection have bolstered trust and facilitated the expansion of ETFs into new markets.

Technological Advancements

Advances in financial technology have streamlined ETF trading and accessibility. Online platforms and robo-advisors have made it easier for investors to include ETFs in their portfolios, further driving adoption.

Broad Market Access

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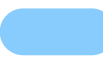







Innovation in Thematic and ESG Investing

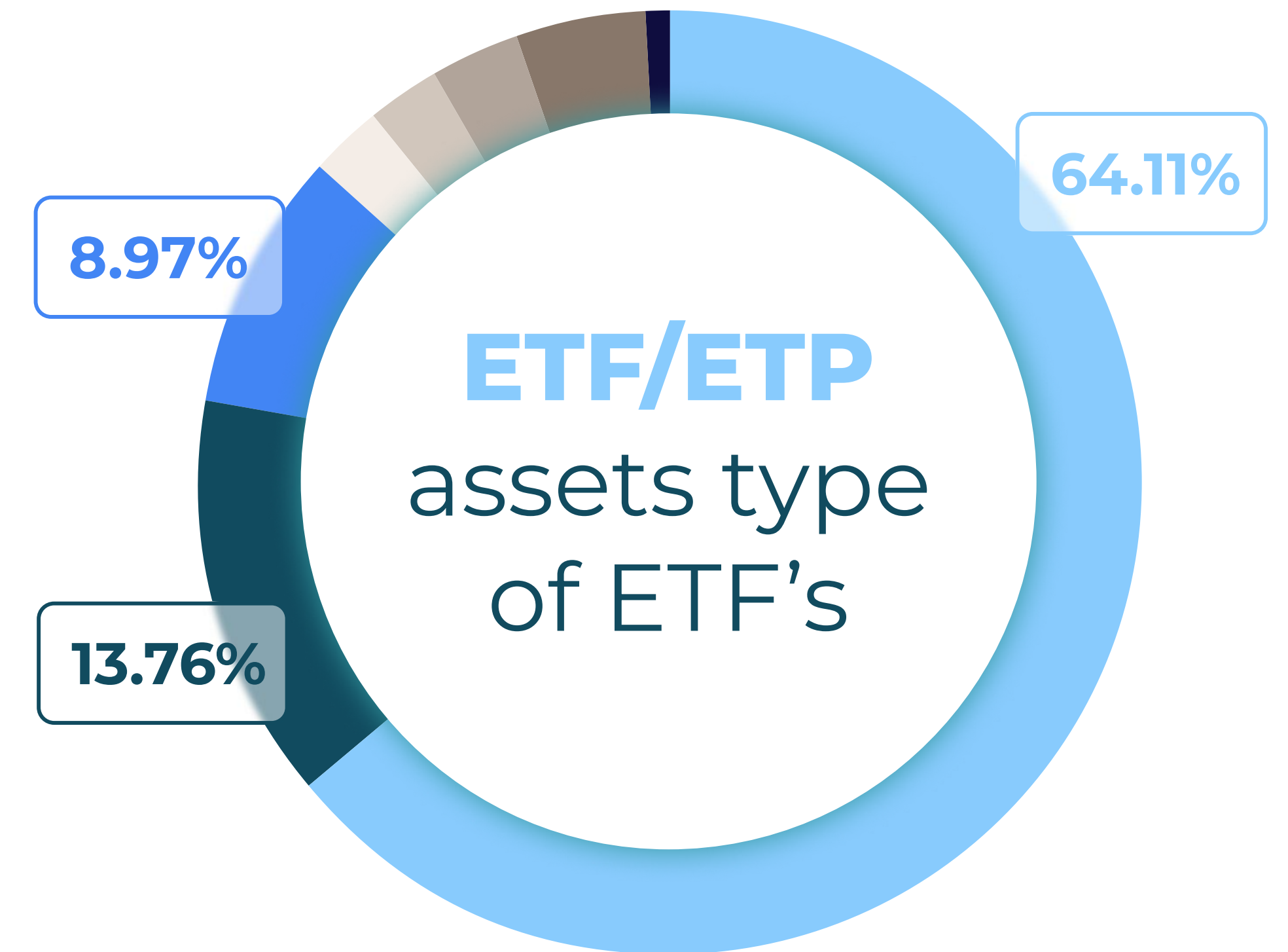
Evolving regulatory frameworks in various jurisdictions have enhanced the appeal of ETFs. Improved regulations around disclosure, trading practices, and investor protection have bolstered trust and facilitated the expansion of ETFs into new markets.

ETFs are well-positioned to provide investors with diversified, cost-effective, and flexible investment solutions. However, it's always important to make data-driven decisions when choosing whether or not ETFs are the best investment type.



Understanding the Different Types of ETFs

Types Of EFT's	#ETF's/ ETP's	Assets (US\$ Bn)	% Total
 Market Cap (Equity)	5,390	7,690	64.11%
 Smart Beta (Equity)	1,351	1,651	13.76%
 Emerging Market Exposure	2,853	1,076	8.97%
 China Exposure (Equity)	1,091	313	2.61%
 Thematic	1,483	279	2.32%
 Currency Hedged	649	356	2.97%
 ESG	1,467	549	4.58%
 Crypto	208	82	0.69%



Market Capitalization ETFs

These ETFs track indices weighted by market capitalization, such as the S&P 500. Market cap ETFs are the most common type, accounting for a significant portion of ETF assets.

Investor Appeal: They offer broad market exposure with low fees, making them a staple in many investment portfolios.

Smart Beta ETFs

Smart Beta ETFs use alternative index construction rules, focusing on factors like value, momentum, size, quality, volatility, and dividend yield. They aim to outperform traditional market-cap-weighted indices by capturing specific risk premia associated with these factors.

Investor Appeal: Provide a middle ground between passive and active investing, potentially offering enhanced returns while maintaining lower costs.

ESG (Environmental, Social, and Governance) ETFs

ESG ETFs invest in companies that meet certain environmental, social, and governance criteria. ESG investing has gained traction, especially in Europe, driven by regulatory support and increasing investor awareness.

Investor Appeal: Allows investors to align their portfolios with their values while potentially benefiting from sustainable business practices.

Thematic ETFs

Thematic ETFs focus on specific investment themes or sectors, such as technology, healthcare, clean energy, or robotics. Interest in thematic ETFs surged during the COVID-19 pandemic as investors sought exposure to sectors poised for growth.

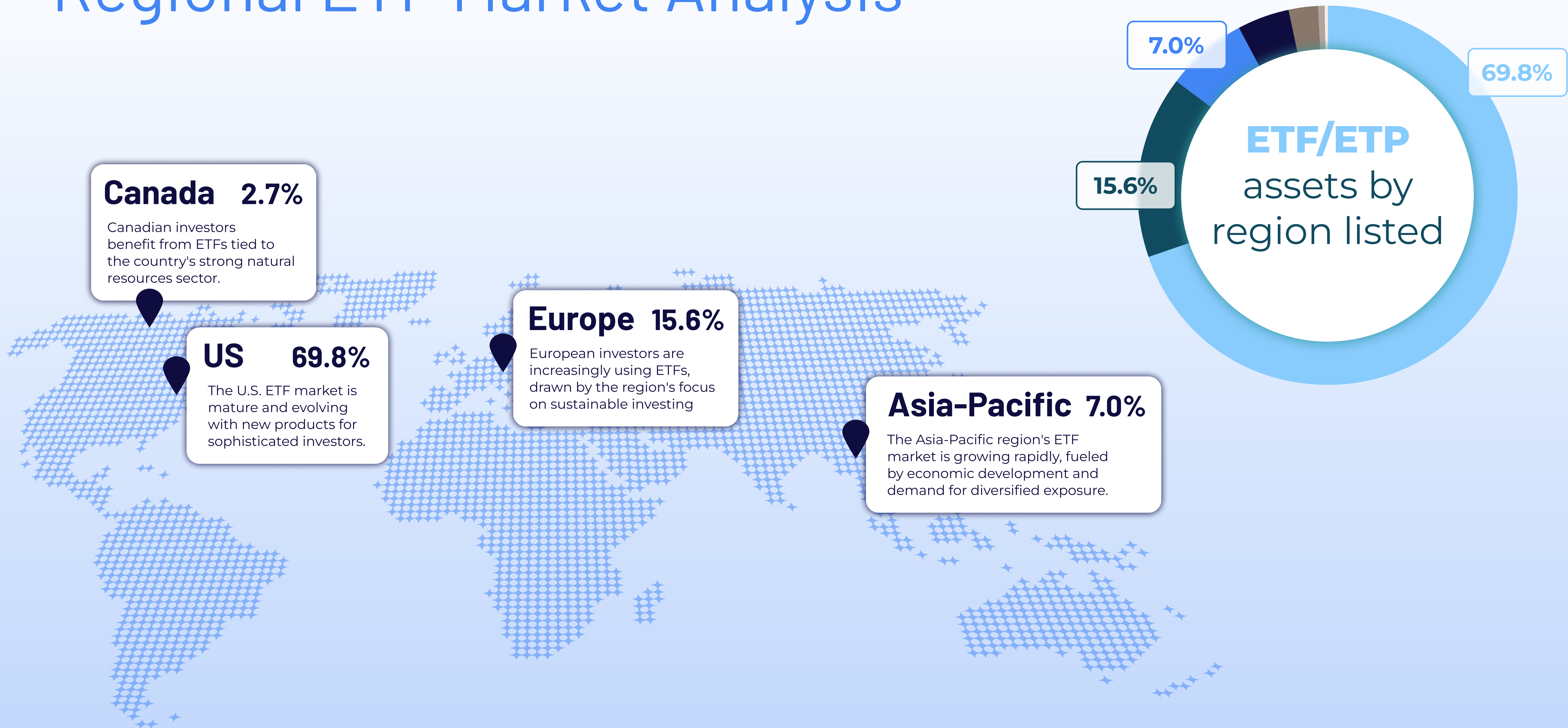
Regional Trends: Particularly popular in Asia and Europe, where investors are keen on capitalizing on emerging global trends.

Active ETFs

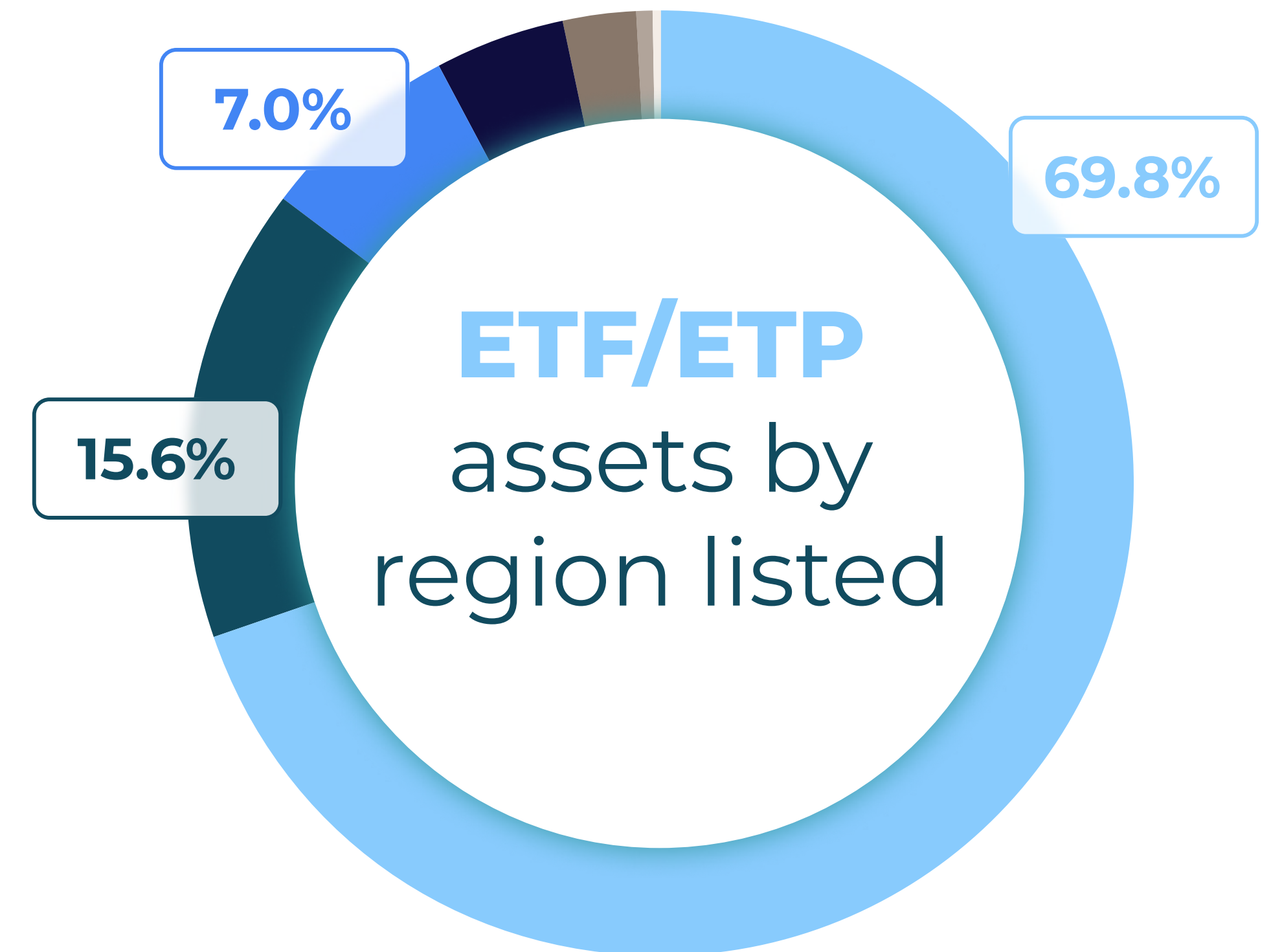
Unlike traditional passive ETFs, active ETFs are managed by portfolio managers who make investment decisions aiming to outperform a benchmark. The rise of active ETFs is propelled by their tax efficiency and flexibility compared to mutual funds. Several mutual fund providers have converted their funds into active ETFs to meet investor demand for more dynamic investment strategies.

Regional Trends: In the U.S., active ETFs have seen substantial growth as investors seek tax-efficient alternatives to mutual funds without sacrificing active management.

Regional ETF Market Analysis



Region	#ETF's/ ETP's	Assets (US\$ Bn)	% Total
US	3,531	8,996	69.8%
Europe	3,032	2,009	15.6%
Asia Pacific	3,414	904	7.0%
Japan	332	563	4.4%
Canada	1,160	345	2.7%
Middle East And Africa	772	48	0.4%
Latin America	130	25	0.2%
Total	12,321	12,890	100%



United States

Investor Base:

- **Retail Investors:** Widespread adoption due to accessibility and variety.
- **Institutional Investors:** Use ETFs for strategic asset allocation and liquidity management.
- **Product Innovation:** Significant growth in active and fixed-income ETFs, catering to diverse investment strategies.

Canada

- **Historical Significance:** Home to the first-ever ETF, setting the stage for global ETF development.
- **Market Characteristics:** Focus on commodities and resource-based ETFs due to Canada's economic landscape.

Europe

Investor Base:

- **ESG Leadership:** Europe leads in ESG ETF adoption due to supportive regulations like the Sustainable Finance Disclosure Regulation (SFDR).
- **Retail Growth:** Increasing engagement through investment platforms and savings plans, making ETFs more accessible to individual investors.
- **Regulatory Environment:** European regulations emphasize transparency and investor protection, fostering confidence in ETF products.

Asia-Pacific

Investor Base:

- **Thematic Investing:** High interest in sectors like technology, healthcare, and consumer trends.
- **Institutional Use:** Sovereign wealth funds and large institutions utilize ETFs for efficient market access.
- **Market Development:** Rapid growth in ETF listings and innovation, with local exchanges promoting ETF adoption.

Emerging Markets

Access via ETFs:

- ETFs provide a practical way to invest in emerging markets, which may have restrictive access or regulatory hurdles.
- **Latin America:** Countries like Mexico, Chile, and Peru are adopting ETFs for international diversification.

Investor Benefits:

- Simplified access without the need for foreign investor status or opening local bank accounts.
- Exposure to high-growth markets with the convenience of local currency trading.



Investor Demographics and Behavior

Institutional Investors

Institutional investors hold approximately 50% of global ETF assets. ETFs provide these institutions with efficient exposure to various asset classes and regions, aiding in portfolio diversification and strategic allocation. For example, the Public Investment Fund of Saudi Arabia seeded an ETF with \$1 billion to gain exposure to specific markets, while the Ministry of Finance in Colombia collaborated with ETF providers to launch local ETFs, enhancing market liquidity. These examples illustrate how institutional investors utilize ETFs for tactical adjustments and to implement specific investment strategies on a large scale.

Retail Investors

Online trading platforms have made ETF investing more accessible to individual investors. The appeal of lower fees and greater transparency attracts cost-conscious retail investors seeking value. Additionally, increased financial literacy and awareness have led more individuals to consider ETFs as viable investment options. In the United States and Asia, high levels of retail participation are supported by well-developed financial markets; in Europe, engagement is growing, although regulatory complexities can sometimes act as a barrier.

Pension Funds and Sovereign Wealth Funds

The rise of thematic ETFs focusing on specific sectors or trends such as technology, healthcare, and clean energy has attracted investors seeking to capitalize on emerging opportunities. Additionally, the growth of ETFs incorporating Environmental, Social, and Governance (ESG) criteria reflects a growing demand for socially responsible investing options.



Best Practices for ETF Selection

1. Define Investment Objectives

Defining investment objectives is a crucial step in the investment process. Investors should first clarify their goals and assess their risk tolerance. Additionally, always consider the time horizon of the investment. Short-term traders may prioritize liquidity, while long-term investors might focus on cost efficiency.

2. Understand ETF Structures

It's important to know the product structure of an ETF - whether it physically replicates the index or uses synthetic replication through derivatives, which can introduce counterparty risk. Also consider the legal structure, as ETFs can be structured differently across regions (for example, U.S. ETFs versus UCITS ETFs in Europe), affecting regulations, tax treatment, and investor protections. Additionally, investors should decide between accumulating (reinvesting dividends) or distributing (paying out dividends) share classes based on their income needs.

3. Evaluate Liquidity & Costs

When assessing liquidity, consider both the trading volume of the ETF and the liquidity of its underlying assets. For large trades, engaging with authorized participants or market makers can ensure efficient execution. Regarding expense ratios, while lower fees can enhance net returns over time, it's important to consider the value provided by higher-cost ETFs offering specialized exposure.

Be mindful of bid-ask spreads as well; wider spreads can increase transaction costs, particularly for frequently traded ETFs. Utilizing limit orders can help control execution prices and manage costs effectively.

Understanding the Risks of ETFs

While ETFs offer a range of advantages, they are not without risks. Investors should carefully evaluate the potential downsides to ensure that ETFs align with their risk tolerance and investment objectives. Below are key risks to be aware of:

Market Risk

As with any equity or fixed-income investment, ETFs are subject to market risk. The value of an ETF will fluctuate based on the performance of its underlying assets, which means that if the broader market or sector experiences a downturn, the value of the ETF may decline in parallel.

Liquidity Risk

Not all ETFs are created equal when it comes to liquidity. Some ETFs, particularly those focusing on niche or emerging sectors, may have low trading volumes, making it difficult to buy or sell shares at desirable prices. Additionally, even if an ETF is highly liquid, the underlying assets it holds may not be, introducing the risk of wider bid-ask spreads and price inefficiencies.

Concentration Risk

While ETFs typically offer diversification, some may have a high concentration of assets in a particular sector, country, or company. This exposes investors to higher risk if that specific area underperforms or faces economic challenges. It's important to assess the concentration within an ETF's holdings to ensure it aligns with the desired level of diversification.

Counterparty Risk (Synthetic ETFs)

Some ETFs use derivatives rather than physically holding the assets they aim to replicate. These "synthetic ETFs" introduce counterparty risk, where the failure of the derivative provider could negatively impact the value of the ETF.

Regulatory and Tax Risks

As with any equity or fixed-income investment, ETFs are subject to market risk. The value of an ETF will fluctuate based on the performance of its underlying assets, which means that if the broader market or sector experiences a downturn, the value of the ETF may decline in parallel.

By understanding these risks, investors can make more informed decisions and ensure that ETFs are part of a broader, well-balanced investment strategy. Just as it is essential to weigh the benefits of ETFs, it is equally important to consider their potential pitfalls to maximize returns and minimize exposure to unnecessary risks.

Know Your Enemy:

Weighing ETFs Against Individual Assets

While ETFs have become an attractive and convenient investment option, it's important for knowledgeable investors to recognize that ETFs are not the only solution for portfolio growth. ETFs often provide a simplified, diversified investment strategy, but they may not always be the most profitable choice, especially for those who are well-versed in analyzing individual assets.

By purchasing ETFs, you are investing in a basket of assets, which can dilute exposure to high-performing stocks. In some cases, selecting individual stocks from the underlying assets of an ETF could potentially yield higher returns, depending on market conditions and the investor's research capabilities. For investors willing to take on more risk and commit to a hands-on strategy, bypassing the "easy" choice of ETFs in favor of direct stock investments might offer superior rewards.

Using an investment intelligence platform helps you develop a deeper understanding of the underlying assets within these funds. Equipped with this knowledge, you can make informed decisions on whether ETFs truly align with your financial objectives—or if it's time to explore alternative paths for maximizing profitability.



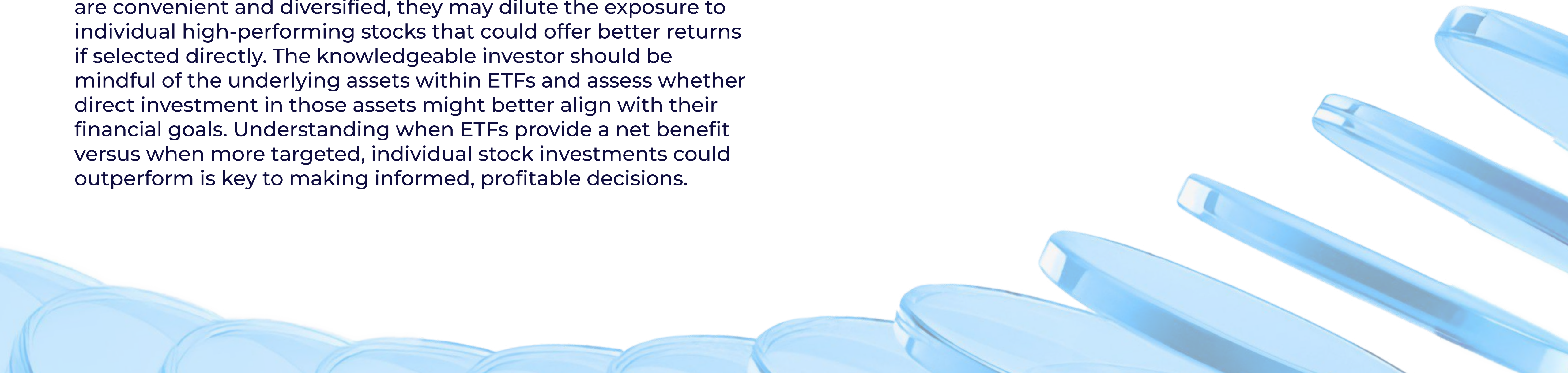
Conclusion

The ETF industry continues to revolutionize the investment landscape. The consistent growth in assets and net inflows underscores the confidence investors have in ETFs. As the industry evolves, staying informed about trends, regulatory changes, and best practices is crucial for maximizing the benefits of ETF investing.

By understanding the various ETF categories, regional market dynamics, investor behaviors, and factors driving adoption, investors can make more informed decisions. Whether for institutional or retail investors, ETFs offer a versatile tool for achieving a wide range of investment objectives.

ETFs are not always the best choice for every investor. While they are convenient and diversified, they may dilute the exposure to individual high-performing stocks that could offer better returns if selected directly. The knowledgeable investor should be mindful of the underlying assets within ETFs and assess whether direct investment in those assets might better align with their financial goals. Understanding when ETFs provide a net benefit versus when more targeted, individual stock investments could outperform is key to making informed, profitable decisions.

ETFs are likely to remain at the forefront of investment portfolios, but knowing when and how to use them effectively will define the success of investors going forward. Investment intelligence platforms offer deeper insights into the underlying assets within ETFs, providing a more sophisticated approach to evaluating whether direct investment in individual stocks may yield better returns.



About

BRIDGEWISE

At Bridgewise, our vision is to create a world where investment opportunities are accessible to everyone, everywhere.

We believe that the benefits of informed investing should be within reach for all, regardless of geographic or linguistic barriers.

To achieve this, we are expanding global investment horizons through advanced AI-based investment intelligence, significantly increasing the coverage of securities worldwide.

Our intuitive and comprehensive solutions, available in any language, are designed to bridge gaps between knowledge and action, data and decisions, and investors and markets.

By delivering actionable insights and recommendations, we help platforms connect their users with new opportunities across the globe.

**Join us as we reshape the future of investing,
where opportunities are limitless and
accessible to all.**