

There's no debating the intelligence of "smart beta"



Rohit Mehta

Exchange-traded funds (ETFs) are continuing their ascent in the Canadian marketplace, which comes as no surprise given their inherent transparency, relatively low cost and liquidity – not to mention their ability to find a comfortable fit in almost any portfolio. From the cautious buy-and-hold investor to the more aggressive opportunity seeker, the ETF universe is expanding to meet the needs of all investor types.

ETFs are becoming more specialized. There is a fairly new type of ETF on the street – one that looks beyond systematic risk (beta) to other factors that tend to impact relative performance. It is called "smart beta." While the use of this term remains contentious (due to the fact that by referring to these as "smart", individuals may perceive traditional ETFs as "dumb"), all smart beta ETF providers have one belief in common: that market capitalization does not capture all of the relevant information about a company's value and potential.

Smart beta ETFs strive

to deliver superior risk-adjusted returns for investors, while addressing concerns that cap-weighted indices will potentially expose them to overvalued stocks and higher volatility. As a result, the smart beta market segment is growing rapidly. Some of the most well-known index providers in the world, including Morningstar, MSCI, and Russell Investments, are focused on creating sophisticated, smart beta indices to meet the evolving needs of investors.

Smart beta indexation is also known as "factor-based" investing. Factors are the empirically validated characteristics of stocks that demonstrate a market-cap-weighted portfolio is not the only, nor necessarily the best, way to hold a portfolio. An investor can use smart beta ETFs as the building blocks in the construction of a portfolio to truly reflect short- and long-term markets, as well geographic outlook. An investor can also tilt the portfolio to help emphasize yield, growth or value, and all with a level of transparency not found from traditional mutual funds. This transparency makes combining smart beta ETFs more efficient – investors always know exactly what's

in their portfolio, how each holding complements one another, and how they are all being managed.

Several of these First Asset ETFs are built using Morningstar® CPMS™ – Morningstar's proprietary equity research platform that integrates fundamental and technical data with analysts' earnings estimates for over 3,600 Canadian and U.S. stocks. First Asset has created ETFs that aim to replicate Morningstar® Indexes using quantitative models that capture value, momentum, or dividend effects for Canadian investors. For example, **First Asset Morningstar Canada Momentum Index ETF** (TSX: WXM) and **First Asset Morningstar Canada Value Index ETF** (TSX: FXM) are designed to provide diversified exposure to Canadian issuers that have demonstrated, among other things, positive momentum in earnings and price (in the case of WXM), and "value" characteristics like low price-to-book and low price-to-earnings (for FXM). For investors who value these highly important qualities when investing in a company, WXM and FXM are effective solutions to replace or supplement a traditional cap-weighted ETF.

First Asset offers other smart beta (factor-based) ETFs that are focused on the volatility factor, including: **First Asset MSCI Canada Low Risk Weighted ETF** (TSX:RWC), **First Asset MSCI Europe Low Risk Weighted ETF** (TSX:RWE), **First Asset MSCI USA Low Risk Weighted ETF** (TSX:RWU) and **First Asset MSCI World Low Risk Weighted ETF** (RWW). All of First Asset's foreign ETFs are available in hedged and unhedged versions.

While debate over the term "smart beta" may remain a topic of conversation for some time, the benefits of incorporating smart beta strategies – or factor-based ETFs – into an investment portfolio are clear. When seeking an indexing strategy that offers the potential for superior risk-adjusted returns, smart beta works.

To learn more about the benefits of "smart beta" and factor-based investing with First Asset ETFs, please contact First Asset Exchange Traded Funds at 1.877.642.1289.

Rohit Mehta

Rohit Mehta brings 15 years of experience in the financial services sector to his role as Senior Vice President at First Asset. He is a contributing speaker at many industry conferences, events, and also is a regular commentator in the media.

www.firstasset.com

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