SCHLINDWEIN ASSOCIATES
INVESTMENT COUNSEL

Choices

Investors do not lack for investment choices. Has the significant proliferation of choices helped improve investment outcomes or made the decision process just more challenging? Proliferation of choices is no more pronounced than among U.S. exchange-traded funds ("ETFs"). Since the launch of the first ETF in 1993, choices now exceed 2,500 funds. Investors have embraced them with combined ETF assets surpassing $6.1 trillion. In and of itself, the ETF vehicle is neither good nor bad. The investment focus of some ETFs may raise questions as could the manner in which investors deploy them in portfolios. A review of ETF dynamics can provide perspective for investing yet ahead.

PERSPECTIVE

The growth in ETF choices is displayed in Chart I. Currently, 2,553 funds are available for investment. From a slow start in the 1990s, rate of annual new launches generally has accelerated and 2021 is on pace for a record launch in excess of 350 new ETFs. Chart I excludes ETFs that were launched and subsequently closed, mostly for not reaching sufficient asset size. This dynamic likely will continue as the ETF market is extremely competitive and as individual fund focuses become more specialized. The average ETF has a robust asset base of $2.4 billion, but this statistic skews perspective. The largest fund exceeds $350 billion. At the same time, 47% of funds have assets of less than $100 million, a level at which survival likely is at risk.

The original and still largest ETF is an index fund managed to track the broad S&P 500 index. Unlike the traditional index mutual fund, the ETF structure gives investors the ability to buy and sell (long or short) shares throughout the trading day. In addition, ETFs offer potential income tax benefits to investors. As displayed in Chart II, ETFs cover the full range of market sectors. Some invest quite like traditional index mutual funds. Others have brought new methodologies to the construction of broad market indexes. Still others have been created to address quite specific market niches. They provide expanded investment choices for alternative investing and for fine-tuning equity sector allocations.

A growing number of ETFs have been launched to provide traditional active portfolio management instead of tracking a market index. Chart III shows the index/actively-managed mix of ETFs. In addition, median expense ratios are shown. The majority of ETFs are index funds but actively managed funds are being launched at a faster pace. The higher median expense ratio for actively managed ETFs approaches that of traditional mutual funds. Index funds generally are associated with low expenses, and some index ETFs carry extremely low expense ratios. However, the more specialized the focus of the index ETF generally the higher the expense ratio as the respective ETF sponsors seek compensation for their proprietary structures.

INVESTMENT IMPLICATIONS

More ETF choices bring more potential opportunity for investors and likely more complexity to their portfolio processes. For more ETFs to enhance portfolio outcomes, each ETF must serve a clear portfolio purpose and any exposure redundancy must be understood. Holding several ETFs with highly overlapping sector and security exposures brings more risk rather than more diversification. Adding actively managed ETFs means added due diligence to achieve portfolio goals.

CHART I

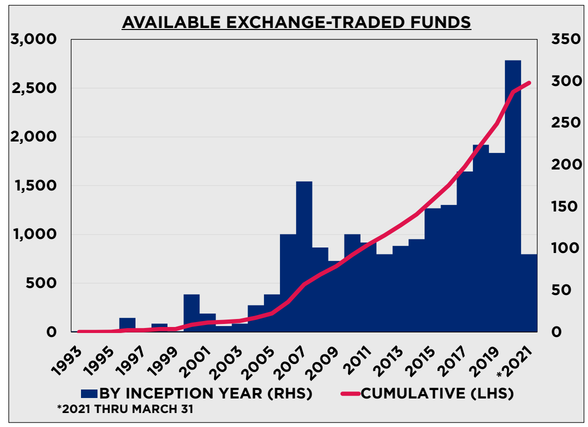

CHART II

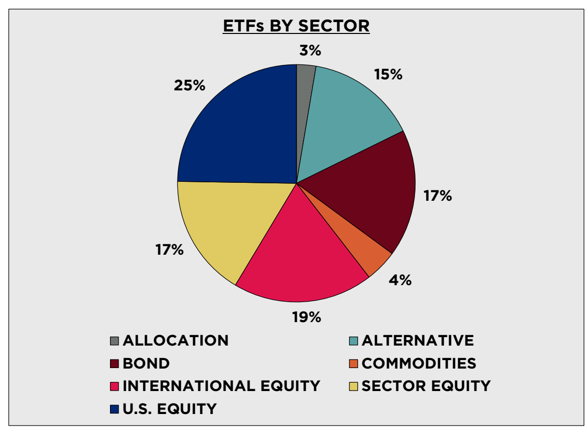

CHART III