

SI Quick Insight: So Far, ETFs Don't Replace Actively Managed Mutual Funds

Exchange-Traded Funds (ETFs) have grown remarkably. U.S. ETF assets totaled \$603 billion at the end of April 2008, up 42% from \$423 billion at the end of 2006. But for now, the majority of ETF use is institutional (hedge funds, mutual funds, etc.). **Among individual investors, more than three-quarters of ETF use represents substitution of ETFs for stock purchases or for Separately Managed Accounts.** In that respect, they're often used for strategic sector bets, short-term trading vehicles, or asset-allocation building blocks.

ETFs					
	Assets				# of Funds
	\$B	Net Flows \$B			
Legal Structure	12/07	2005	2006	2007	12/07
Open-End Fund	440.9	53.2	67.5	104.0	593
UIT	139.2	-2.5	-8.7	33.9	8
Grantor Trst / Ptnrshp	28.6	3.1	8.5	8.9	28
ETN	4.7	0.0	1.1	2.8	25
Total	613.4	53.7	68.5	149.5	654

Source: Strategic Insight Simfund MF

With more than 100 ETFs at \$1 billion-plus in size, the products often provide liquid solutions for institutional investors looking to park cash in equities, or looking for hedging alternatives to futures (as well as risk management tools to add or reduce duration risk to portfolios). In the retail world, ETFs face the obstacle of little presence (for now) in DC plans, which are the destination of roughly two-thirds of equity fund flows.

ETFs can offer cost advantages, and they continue to fuel innovation. Bond ETFs are a new area of growth, as are specialized currency- and commodity-based products; also, the first ETF-of-ETF products recently launched. However, simple **asset-class exposure continues to dominate individual retail use of ETFs.** Even the first actively managed ETFs, launched this year, are rather passive asset-exposure vehicles.

We continue to see retail investors use mutual funds as the foundations of their portfolios. Retail use of ETFs is growing slowly, and will continue to do so in the near future.

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