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Now Available:

In-Depth Report on

ETFs: Growth, Innovation, Competition

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Report details:

* 190+ pages
* 50+ tables and charts
* On sale Feb. 2009
* Buyers of this study will also receive quarterly ETF data updates during 2009

Strategic Insight is pleased to announce its in-depth report on Exchange-Traded Funds (ETFs). ETFs are among the most innovative investment products of the past generation, and have been generating much interest lately due to their low cost, tax efficiency, range of asset-class categories, and intraday tradeability. ETFs have continued growing in the difficult market environment of 2008, drawing inflows of more than $260B globally, reaching more than $725B of assets in the US, Europe and Asia. But how do ETFs complement and compete with traditional mutual funds? How do ETFs change the way advisors manage individuals' money?

This report, centered on the US but offering details on ETFs around the world, covers the growth of ETFs, the diversity of ETF product strategies, ETF distribution, products in the pipeline, the future direction of the ETF space, and more.

The topics to be covered include:
* Trends in flows and asset growth
* Product development and innovation
* Who uses ETFs and why
* ETF distribution strategies
* The potential of actively managed ETFs
* ETFs in Europe and Asia
* ETFs vs. traditional mutual funds
* Prospects and challenges for future ETF growth

The report is based on research using proprietary surveys, extensive discussions with executives and advisors at all levels of the industry, Strategic Insight's Simfund databases, and SEC filings.

The study is a must-read for any firm that is actively engaged in managing ETFs, considering the launch of ETFs, or just trying to better understand the role of these products in the marketplace and their competitive position versus mutual funds. The comprehensive data provide key intelligence on various aspects of the products, and will include detailed assets, flow and other information.

ETFs:
Growth, Innovation, Competition

Strategic Insight*

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* Refers to Strategic Insight Mutual Fund Research and Consulting Electronic Products Inc. and its wholly-owned subsidiary, Strategic Insight Mutual Fund Research and Consulting LLC, both defined as Strategic Insight.

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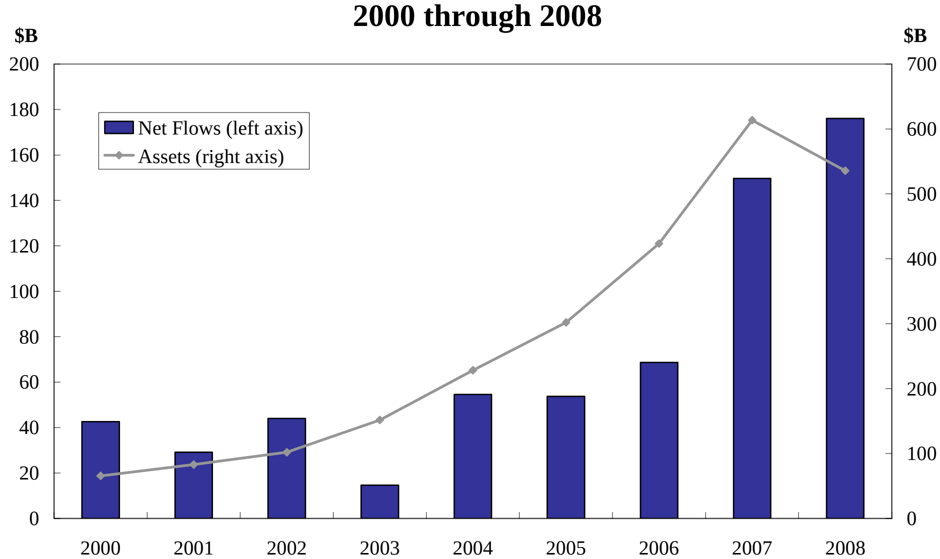
Executive Summary

We have divided this report on Exchange-Traded Funds (ETFs) into nine chapters, with each chapter surveying various aspects of a broad topic. The business of ETFs is complicated, and so below we lay out some of the key findings and themes that we expand upon in this report. Several factors are reshaping the investment management landscape now and in the coming years, and the ETF is a key part of this evolution.

- Exchanged-Traded Products (ETPs), which include ETFs, trusts and ETNs, have grown tremendously since the debut of the first ETF in 1993. US-listed Exchange Traded Products held more than half a trillion dollars at the end of 2008, and drew $176 billion in net inflows last year, impressive gains in a very difficult market environment. And ETFs in Asia and Europe captured more than $80 billion. Indeed, the ETP business has grown steadily through bull and bear markets.

US Exchange-Traded Products Growth
2000 through 2008



Source: Strategic Insight Simfund MF

- Growth has been propelled by a broadening of the buyer pool, with awareness, acceptance and usage of the ETP structure rising among both institutional and retail intermediary-driven and individual clients.

- The three leading players in the US ETF business are: Barclays Global Investors (BGI), which has the most ETFs and the most assets; State Street Global Advisors (SSgA), which launched the first US ETF in 1993 (the S&P 500 SPDR) and is now the second-largest sponsor; and Vanguard, the indexing giant that entered the business in 2001 with ETFs structured as share classes of its index funds.

- The volume of ETF growth has brought with it a flowering of diverse investment strategies. There are now some 800 different ETFs trading in the US. And investors can use them to track everything from US large cap stocks to Brazilian stocks, from gold to revenue-weighted versions of popular stock indexes. ETPs started since the beginning of 2006 account for three-quarters of all ETPs, driven by both existing players fleshing out their lineups and by new entrants. Among the areas of growth have been inverse and long-leveraged ETPs, whose US assets have topped $22 billion. (The broadening of the array of ETP products available has also come with some consolidation.)

- A growing piece of the industry is in using ETFs as building blocks for multi-asset class portfolios, including lifecycle-based and tactical allocation strategies, implemented within regular single ETFs, or funds-of-ETFs, and ETFs-of-ETFs – with efforts from BGI, TD Ameritrade, PowerShares and others.

- After many years of development, 2008 saw the US launch of the first “actively managed” ETFs, which do more than just track an index. At the end of December there were 13 active ETFs with about $240 million in assets. More “transparent” active ETFs are in the pipeline, and several firms have filed for ETFs that would more closely resemble a fully active mutual fund (in January 2009, Grail Advisors and American Beacon registered two active ETFs that would be run like traditional, actively managed equity funds). Active ETFs will no doubt be attractive to some mutual fund firms, but they will face some challenges.

- The industry has also seen some growth in Exchange Traded Notes (ETNs), which are essentially “ETF-like” debt instruments that don’t hold underlying securities. At the end of 2008, US ETNs held roughly $4 billion in assets, with the vast majority of those assets in commodity- or currency-based notes. Barclays, the first ETN issuer, dominates the ETN space but other competitors are growing. Concerns about issuer credit risk have risen, slowing the growth of ETNs.

- The simultaneous growth in the industry of asset allocation and fee-for-advice compensation models help support ETF growth. More investors see ETFs as vehicles for beta exposure in asset-allocation. And expanded use of fee-based distribution creates a larger framework within which financial advisors can use ETFs, which lack trailing revenue.

- The ability to trade ETFs intraday is a key feature for institutions and some FAs, and recent market turbulence has highlighted ETFs as trading vehicles. ETF trading in November accounted for more than 40% of all US equity trading. The biggest, most liquid ETFs are consistently among the most heavily traded securities in the US.

- Some 40% to 50% of ETF assets reside with institutions, based on information gleaned from large ETF sponsors. These institutions include pension funds, hedge funds, endowments, foundations, proprietary trading desks, and mutual funds. And 50% to 60% of ETF assets reside with retail users, including financial advisors and the direct retail channel. At some large ETF sponsors, new ETF sales are skewing a little more heavily toward retail than institutional. This suggests a gradual deepening and broadening of the retail ETF market.

- Operational challenges have meant ETFs have achieved little penetration yet within DC plans. Efforts to fit ETFs into 401(k) plans include programs from WisdomTree, recordkeeping firm Invest n Retire, and collective trusts using ETFs. In the coming years, we do see potential for greater use of ETFs, initially, in small- and mid-cap DC plans.

- Registered Investment Advisors (RIAs), the early retail adopters of ETFs, generally plan to boost their use of ETFs in the next two years, according to SI's proprietary survey. RIAs that use ETFs see them as competing with open-end mutual funds, index funds and individual stocks, using ETFs in both core and satellite holdings in "core-satellite" portfolios, our survey found.

- ETF use is growing even faster in Europe, a mostly institutional market, than in the US. Similar asset-allocation trends are helping the younger ETF industry there, as are regulations that make it easy to cross-list certain ETFs on many exchanges. Asia also holds much potential for the ETF business, but the uptake of passive vehicles in the region has been slower.

- For now, we estimate maybe 70% of ETFs use by individuals represents substitution of stocks/separately managed accounts, and not of actively-managed mutual funds. This view is based on our discussions with executives at various points in the ETF manufacturing, distributing and trading processes. However, this mix is gradually changing as ETFs penetrate deeper into the investment world. While ETFs are only slowly emerging as substitutes for actively managed mutual funds, their potential is already pressuring managers of traditional mutual funds.

- After $176 billion of 2008 inflows, it seems inevitable that US ETF assets, already topping the $500 billion level, will reach the $1 trillion milestone within several years. Market appreciation in the near term is uncertain, and compensation issues limit how quickly broker-dealers will adopt ETF use. But further expansion is certain. A wild card is how well actively managed ETFs are received in the next few years. And with more than $725 billion in global ETF assets at the end of 2008, according to SI's Simfund databases, worldwide ETF assets should eclipse the $1 trillion mark within two years.