





ETF due diligence: What to factor in

to due diligence. But fund selectors need to receive good guidance on what to look out for, especially in a fast-growing area like index-based investing. Here we look at the factors to consider when choosing an ETF and its underlying index.

There is no such a thing as too much information when it comes

ELEMENTS TO CONSIDER WHEN PICKING AN ETF:

ETF



LIQUIDITY The liquidity of an ETF

determines its tradability and influences the total cost of ownership. Also, an ETF's liquidity reflects the liquidity of the underlying securities.

The structure of an ETF will

ETF STRUCTURE



determine how well it can mitigate risks and support liquidity. It is useful to know the fund's investment approach, AUM, top holdings, securities lending practices and how closely it tracks its benchmark.



ETF costs are typically lower than those of comparable

COSTS

mutual funds. Other than the expense ratio, costs may include trading fees.



PROVIDER

provider in the ETF market is essential, as it gives a competitive advantage over other firms in terms of AUM.

The reputation of a fund

INDEX



Understanding an index's

benchmark means determining if a certain ETF meets a client's objective. Investors should know how recognized and trackable an index is and whether it is concentrated in particular sectors, companies or countries.



govern how an index works is critical to establishing how it will perform. Possible methodologies include market capitalization, fundamental weighting, price weighting and equal weighting.

TRANSPARENCY



often an index rebalances, how long it has existed for and how frequently holdings are disclosed.

Users need to know how

principles and that's not only in the published rules that we use to rebalance the indexes, but also in the governance process any time there's a change to the index." ROLF AGATHER MANAGING DIRECTOR, NORTH AMERICAN RESEARCH, FTSE RUSSELL

"Transparency is one of our key

FTSE Russell can help wealth advisors and ETF developers to understand the nature of the indexes we provide, enabling advisors to efficiently assess funds and make better informed decisions for their clients.

Here are some rules to consider:

HOW TO LEARN ABOUT INDEXES:

DATA EXAMPLE From index research to Available data sets exists for categories including supporting trading and equity, fixed income, corporate actions and dividends,

Analytics include ETF data, adaptive asset allocation policy calculators and PCBond analytics.

reporting, FTSE Russell

shares key insights for better decision making.

ANALYTICS TOOLS A toolbox to inform asset

sustainability and industry classification benchmark.

DESIGN METHODOLOGY

objectives.

to meet certain objectives, such as diversification. For an index to be investable, it is important that their methodology closely meets those

Indexes can be designed

The Russell 2000® Index has the objective to track the

The FTSE Global Equity Index Series offers a consistent

allocation strategies,

manage risk and examine market conditions to help achieve better risk-adjusted returns.

and flexible capping methodology to help investors meet concentration and diversification requirements

performance of the smallest 2,000 US companies in

the Russell 3000° Index, measured by market cap.

OBJECTIVES

TRANSPARENCY Indexes need to be

designed with clear

goals, including how they will achieve targeted factor exposures and

how they will follow those goals in practice.

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