

## Using Exchange Traded Funds

The unique attributes and benefits of ETFs appeal to both institutional and individual investors. Typically structured like mutual funds, but listed and traded on an exchange like stocks, ETFs are flexible trading and investment vehicles that can be used to help satisfy a number of critical investment needs.

### ASSET ALLOCATION

Savvy investors are discovering what institutional investors have known for some time: asset allocation, not security selection, helps drive long-term investment results. However, advanced asset allocation strategies have been difficult for many individual investors to implement, given the costs and asset size required to achieve proper levels of diversification.

The introduction of ETFs now offer investors a sophisticated tool to efficiently gain exposure to broad market segments, encompassing a wide range of asset classes, equity market capitalizations and sectors. This enables investors to build customized investment portfolios consistent with their financial needs, risk tolerance and investment horizon. It's important to remember that diversification and asset allocation do not ensure a profit or guarantee against loss.

### SAMPLE USES

#### STRATEGIC ASSET ALLOCATION

Research shows that a properly allocated portfolio is the most critical factor in explaining the difference in returns across portfolios. The value of asset allocation has been witnessed at most during and after the global financial crisis.

After an investor decides what its long term asset allocation will be, i.e. equities vs. fixed income vs. commodities, it can then utilize passive investment vehicles like ETFs to provide easily managed, low cost proxies for the broader asset markets.

#### CORE-SATELLITE STRATEGY

Investors can also use ETFs to achieve their core-satellite strategy by holding relatively stable and diversified investments as their "core" holdings to form a shock absorber and add "satellite" positions around their core investments in the hopes of generating alpha.

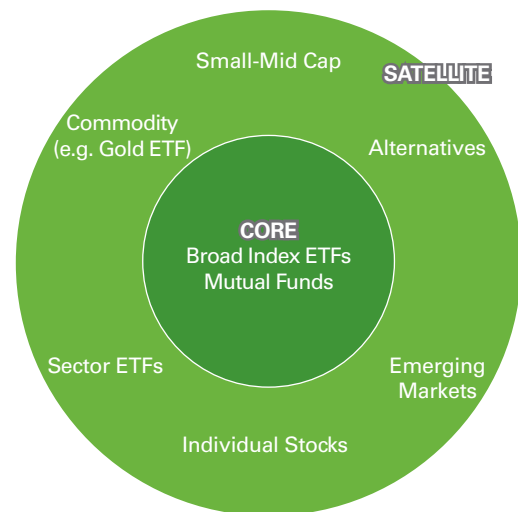
Broad-based ETFs can be used as the core of an investment strategy and complemented with other style- and sector-specific ETFs or mutual funds.

Sector-, commodity-based or other ETFs that track "satellite" asset classes can be used as a cost-effective and efficient complement to a "core" investment in a separately managed account, mutual fund or broad benchmark ETF.

### TACTICAL ASSET ALLOCATION

In today's ever changing macro and geo-political environment, investors often need to make real-time adjustments to their long term asset allocation to reflect changing views on short term asset class performance. ETFs provide a fast and efficient vehicle to access markets to help facilitate these tactical adjustments. Investor can also unwind the positions just as easily as when they were first implemented, after the effects that motivated the tactical adjustment have run their course.

**FIGURE 1: A SAMPLE CORE-SATELLITE STRATEGY**



## RISK MANAGEMENT

ETFs are an attractive hedging vehicle because they can be sold short. Portfolios that have exposure to certain markets can purchase or short sell an ETF in that particular market to hedge against risk. Investors can counter risk by taking the opposite position with the correlating ETF.

The use of short selling entails a high degree of risk, may increase potential losses and is not suitable for all investors. Please assess your financial circumstances and risk tolerance prior to short selling.



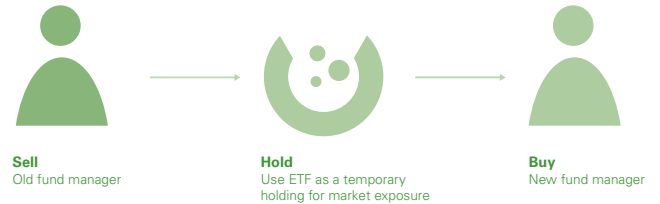
1. Short seller borrows ETF shares from a lender
2. Short seller sells ETF shares
3. Short seller repurchases ETF shares ideally at a lower price
4. Short seller returns ETF shares to lender
5. Ideally short seller keeps profit
6. An investor makes money only when a shorted security falls in value.

## SAMPLE USE

An investor in Singapore has identified SGD1 million worth of diversified long investments, but has only identified SGD 200,000 in single stocks to be short, this would result in SGD 800,000 of net exposure to the market. If he is bullish this may be perfectly fine, however if he is uneasy about the market's short term prospects an ETF that tracks Straits Times Index could be sold short (subject to securing a proper borrow) to reduce the portfolio's net exposure.

## TRANSITION MANAGEMENT

When investors change asset managers, they are often concerned with how to preserve their exposure during the transition. One way to achieve this goal is to liquidate the portfolio and re-invest the assets in an ETF with a high correlation to the benchmark of the active manager. Once established, the new manager can then sell the ETF shares to fund the purchase of the new portfolio's holdings.\*



## SAMPLE USE

An investor is no longer satisfied and decides to terminate the current investment manager of his active large cap portfolio. Until he identifies a new active manager, he temporarily chooses to place his assets in an index ETF. This will maintain proper asset allocation exposure and limit cash drag until a new manager can be identified.

Once he selects a new manager, his ETF portfolio can be easily sold and the proceeds can be used to fund the new active manager.

\* Liquidating a portfolio and re-investing the assets could incur additional costs such as fees, expenses and possible tax consequences. Additionally, the investment return and principal value of your investment could fluctuate in value, so that when shares are sold or redeemed they may be worth more or less than when they were purchased.



#### **ABOUT SPDR® ETFs**

Offered by State Street Global Advisors, SPDR ETFs are a family of exchange traded funds that provide investors with the flexibility to select investments that are precisely aligned to their investment strategy. Recognized as an industry pioneer, State Street Global Advisors created the first ever ETF in 1993 - the SPDR S&P 500<sup>®1</sup>, which is currently the world's largest ETF.<sup>2</sup> SSGA introduced Singapore's first local ETF when it launched the SPDR Straits Times Index ETF in 2002. Currently, State Street Global Advisors manages approximately US\$265 billion of ETF assets worldwide.<sup>3</sup>

For comprehensive information on our ETFs, visit us at [spdrs.com.sg](https://spdrs.com.sg).

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<sup>1</sup> The fund is offered for sale in limited jurisdictions only.

<sup>2</sup> Bloomberg, as of 30 June 2011.

<sup>3</sup> As of 30 June 2011. This AUM includes the assets of the SPDR Gold Trust (approx. \$58 billion as of 30 June, 2011), for which State Street Global Markets, LLC, an affiliate of State Street Global Advisors, serves as the marketing agent.

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The investment return and principal value of an investment will fluctuate in value, so that when shares are sold or redeemed they may be worth more or less than when they were purchased.

Frequent trading of ETFs could significantly increase commissions and other costs such that they may offset any savings from low fees or costs.

In addition to the normal risks associated with equity investing, narrowly focused investments and investments in smaller companies typically exhibit higher volatility.

Foreign investments involve greater risks than US investments, including political and economic risks and the risk of currency fluctuations, all of which may be magnified in emerging markets.

Funds investing in a single sector may be subject to more volatility than funds investing in a diverse group of sectors.

Diversification does not ensure a profit or protect against loss.

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