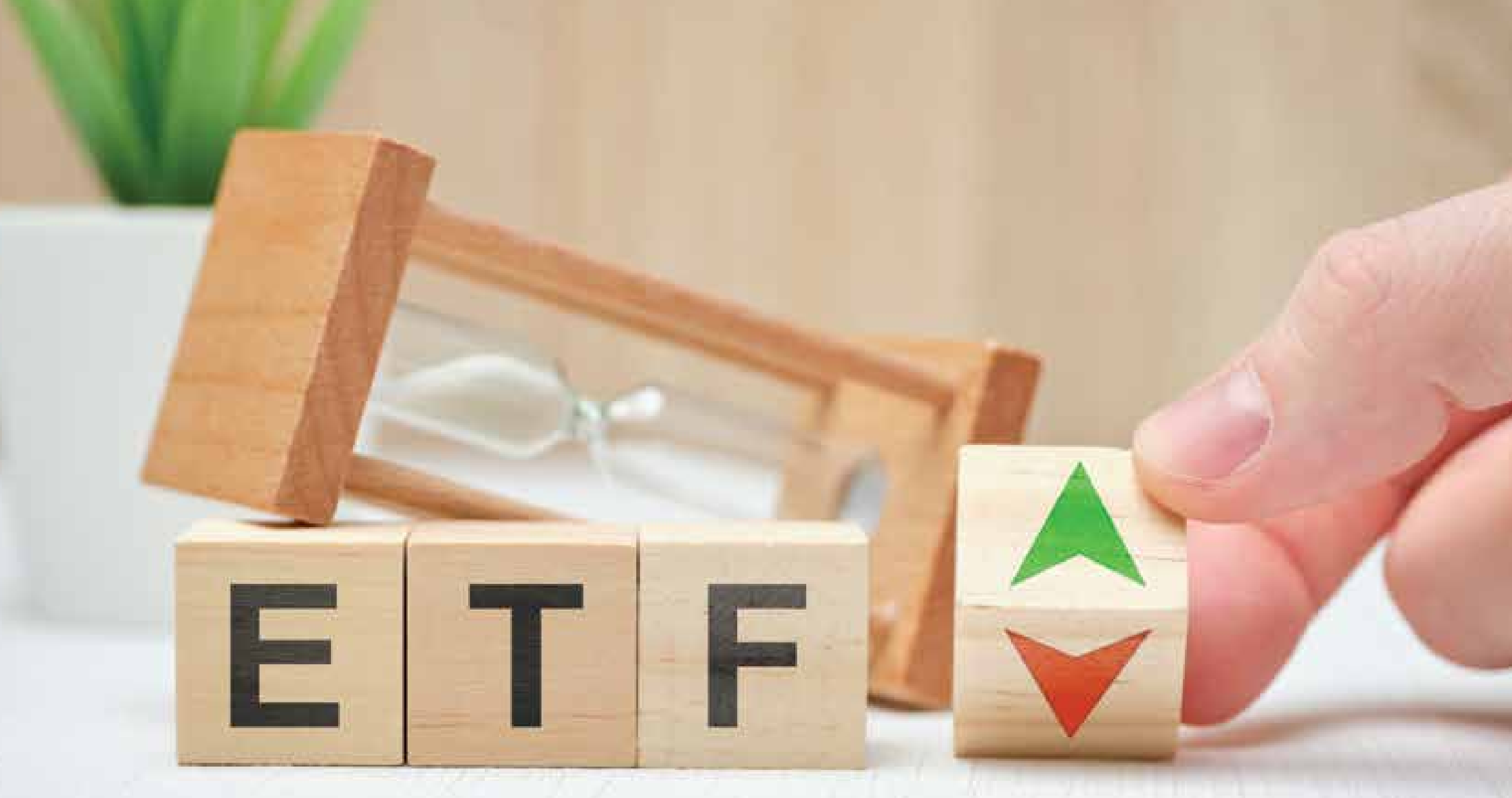

Invest Intelligently with Smart Beta ETFs

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Smart beta exchange traded funds (ETF) have gained increasing prominence amongst investors by combining the best of both active and passive strategies. Today, more investors are making use of these sophisticated investment tools as building blocks in their portfolio to reap better risk-adjusted returns.

After a long wait, Malaysian investors will finally be able to access these products following the listing of 2 Smart Beta ETFs (i.e. TradePlus MSCI Asia ex Japan REITs Tracker and TradePlus DWA Malaysia Momentum Tracker) on the local bourse. But what's so 'smart' about smart beta ETFs? Are they really that intelligent?

In this article, we'll explore what smart beta ETFs are and how do they fit in an investor's portfolio.

01 What are smart beta ETFs?

Smart beta ETFs are innovative forms of ETFs that apply a series of **objective factors** when selecting its component companies. These factors could include different characteristics of a stock like its earnings growth, price momentum or dividend yield.

It differs from **traditional ETFs** that employ a **market-cap approach** towards picking its component companies. It is typically biased towards a stock with a larger market capitalisation as it would constitute a larger weight in an index.

As such, smart beta ETFs would disregard the stock's market-cap and only invest in companies that exhibit certain behaviour or metrics.

02 Types of Factors

Value
Refers to the tendency of cheaply priced stocks outperform pricier stocks in the long term

Momentum
Refers to the tendency of winning stocks to continue to do well in the near term

Quality
Captures companies with durable business models and sustainable competitive advantages

High Yield
Gains exposure to companies that appear undervalued and have demonstrated stable and increasing dividends

Minimum Volatility
Involves buying stocks based on the estimate of their volatility and correlations with other stocks

Source: MSCI, 2020

03 What are its advantages?

By doing away with the traditional market-cap approach towards index investing, smart beta ETFs allow investors to discover hidden opportunities in the marketplace and uncover value.

Smart beta ETFs apply a series of objective and rule-based strategies to screen each index component companies, which are then ranked and weighted according to these specific factors. These factors could be a range of financial metrics like earnings, price momentum or dividend yield. This helps overcome the main disadvantage of plain-vanilla ETFs which are biased towards larger-cap stocks because they constitute a larger weight in an index.

Instead with smart beta, a more objective and systematic approach to investing is employed by considering specific objective factors to decide which companies to invest. These strategies are known to have beaten the market over the long term as it seeks to exploit market anomalies and mitigate the challenge of traditional market cap-weighted ETFs.

Chart 1:Smart beta combines active and passive strategies

PASSIVE	SMART BETA	ACTIVE
• TRADITIONAL MARKET-CAP WEIGHTED ETFS • PASSIVE INVESTING BY TRACKING BENCHMARK • LARGE-CAP BIAS • PROVIDES BENCHMARK/MARKET RETURNS	• SMART BETA ETFS • COMBINES ACTIVE & PASSIVE STRATEGIES • INVEST USING FACTORS (E.G. EARNINGS, DIVIDEND, MOMENTUM) • CUSTOMISED INDEX	• UNIT TRUST FUNDS • ACTIVE STOCK SELECTION AND RISK MANAGEMENT • USES HUMAN JUDGEMENT • AIMS TO OUTPERFORM THE INDEX

04 How do smart beta ETFs fit in a portfolio?

With its cost-effectiveness, smart beta ETFs are ideal building blocks for investors to **construct a diversified portfolio by piling on different strategies** or styles.

By employing a range of different factors such as price, earnings or yield - smart beta ETFs allow investors to build a strong foundation for their portfolio by providing greater diversification.

This allows investors to complement a range of strategies in their investments to minimise risk and reap higher returns at lower volatility.

For example, you can consider complementing your portfolio needs through an array of smart beta strategies such as dividend factors to provide a measure of stability through consistent dividend pay-outs.

Alternatively if you are feeling more opportunistic, you can employ smart beta ETFs that use momentum factors to capture stocks with the highest price momentum.

05 Getting Smart with Smart Beta

By capturing the best of both active and passive strategies, it is no wonder that smart beta ETFs have become increasingly popular for investors today.

Coupled with its low-cost attractiveness, smart beta ETFs can be efficient ways to fill gaps in your portfolio especially if you don't know whether an active or passive approach works best for you.

Leverage the power of smart beta and find out how you can build a resilient portfolio to ride out volatility in the new normal.

Visit https://www.tradeplus.com.my/ to learn more about our latest smart beta ETF offerings.

Be smart about your investments today with smart beta ETFs!
