ETFs Fact or Fiction: Are ETFs Riskier Than Mutual Funds?

For over 20 years, ETFs have grown to become an extremely popular choice for investors seeking a cost-effective option for executing both short-and long-term investment strategies. Understanding how ETFs work and their unique characteristics is an important step toward determining whether ETFs can be an appropriate choice for your portfolio and the role they may play in helping you achieve your own investment objectives.

ETFs combine the benefits of traditional index mutual funds and individual securities. Like index mutual funds, ETFs allow investors to track more than hundreds of domestic and international indexes, including the Straits Times Index and S&P 500®, as well as specific sectors or industries (e.g, Gold). And like individual stocks, ETFs give investors the flexibility to buy and sell on the major stock exchanges throughout the day, at the market price. Investors can also place stop loss and limit orders on ETFs.

Other key differences between ETFs and mutual funds include how they are created and redeemed, how they are priced, the minimum investment required and how they are taxed.

While ETFs and mutual funds have significant differences, they also share many of the same characteristics. Both fund structures are subject to strict oversight and regulation, and the level of risk for both ETFs and mutual funds is ultimately determined by the underlying holdings in the fund.

There is no significant investment research that proves that ETFs carry significantly higher or lower risk than mutual funds. Because most ETFs are designed to replicate the performance of an associated index, their overall risk level should not be significantly higher or lower than that of the index.

The risk and volatility level of any commingled investment vehicle, whether it is an ETF or a mutual fund, is determined by a number of factors, including:

The performance characteristics of the fund's underlying holdings.

Each asset class carries its own level of risk and expected rate of return. By constructing a diversified portfolio that invests in multiple asset classes and investments across the risk-return spectrum, investors can potentially reduce the negative effects of higher risk assets held in a portfolio. Investors should also keep in mind that neither asset allocation nor diversification can ensure a profit or guarantee against loss.

Figure 1: Comparing ETFs to Individual St ocks and Mutual Funds

	Trade Throughout the Day	Flexible Trading Options	Track an Index	Pricing	Minimum Investment
ETFs	•	•	•	Market price	No minimum required
Index Mutual Funds	—	—	•	Closing Net Asset Value (NAV)	Some require minimums
Individual Stocks	•	•	—	Market price	No minimum required

Unlike a stock, Index ETFs and mutual funds are managed funds that follow a passive investment strategy, attempting to track the performance of an unmanaged index of securities. As a result, the Funds may hold constituent securities of the Index regardless of the current or projected performance of a specific security.

ETFs trade like a stock and will fluctuate in market value over the course of the trading day, unlike an index mutual fund. ETFs may trade at prices below or above the ETF net asset value. Buying shares of an Index ETF, similar to buying a stock, will typically involve brokerage commissions to which index mutual funds may not be subject.

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The inherent volatility and risk of the markets or sectors in which the vehicle invests.

Prudent long-term investors know that markets go up and down over time. They also understand that even the most seasoned investment professionals find it next to impossible to time these swings in the market. The portfolios best equipped to weather changing market cycles don't omit stocks or entire segments of the equity markets simply because of their potential risk. Remaining invested over the long term can help investors ride out market cycles and take advantage of potentially lower purchase prices and the impact of compounding.

The investment style the fund uses.

Striking the right risk-reward balance in a portfolio is critical to long-term success. Higher risk portfolios may capture large gains when the market climbs, but these portfolios may suffer heavy losses during a market downturn. On the other hand, lower risk portfolios may not deliver the returns investors need to keep pace with inflation or their spending goals.

In the case of actively managed funds, the manager's bets on individual securities or sectors.

Unlike passive managers, active managers will not seek to match the risk and return profile of an index. Active managers try to identify market opportunities and exploit potential pricing inefficiencies to obtain excess return.

Investors should evaluate their level of comfort with the unique risk and volatility characteristics of a given index, industrial sector or asset class of interest before investing in an associated etf, just as you would when investing in a mutual fund.

Index Definitions

Straits times index The straits times index (STI) is a capitalization-weighted stock market index that is regarded as the benchmark index for the singapore stock market. It tracks the performance of the top 30 companies listed on the singapore exchange. It is jointly calculated by singapore press holdings (SPH), singapore exchange (SGX) and ftse group (FTSE).

Source: Straitstimes.Com.

S&P 500® index The S&P 500 index is an unmanaged index of 500 common stocks that is generally considered representative of the us stock market. The index is heavily weighted towards stocks with large market capitalizations and represents approximately two-thirds of the total market value of all domestic common stocks. The S&P 500 index figures do not reflect any fees, expenses or taxes.

Source: Standardandpoors.Com

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The value of funds may fall or rise and past performances of the funds are not indicative of future performances. Distributions from the funds may be contingent on dividends paid on underlying investments of the funds and are not guaranteed. Listing of the funds on relevant stock exchanges does not guarantee a liquid market for the units and the funds may be delisted. Investors should read the relevant funds' prospectuses for further details including the risk factors

Passively managed funds invest by sampling the index, holding a range of securities that, in the aggregate, approximates the full Index in terms of key risk factors and other characteristics. This may cause the fund to experience tracking errors relative to performance of the index.

Actively managed funds do not seek to replicate the performance of a specified index

The Strategy/fund is actively managed and may underperform its benchmarks. An investment in the strategy/Fund is not appropriate for all investors and is not intended to be a complete investment program. Investing in the strategy/Fund involves risks, including the risk that investors may receive little or no return on the investment or that investors may lose part or even all of the investment.

Diversification does not ensure a profit or guarantee against loss. There can be no assurance that a liquid market will be maintained for ETF shares. Frequent trading of ETF's could significantly increase commissions and other costs such that they may offset any savings from low fees or costs.

ETFs trade like stocks, are subject to investment risk, fluctuate in market value and may trade at prices above or below the ETFs net asset value. Brokerage commissions and ETF expenses will reduce returns. Asset Allocation is a method of diversification which positions assets among major investment categories. Asset Allocation may be used in an effort to manage risk and enhance returns. It does not, however, guarantee a profit or protect against loss.

In general, ETFs can be expected to move up or down in value with the value of the applicable index. Although ETFs may be bought and sold on the exchange through any brokerage account, ETFs are not individually redeemable from the fund. Investors may acquire ETFs and tender them for redemption through the fund in creation unit aggregations only, please see the prospectus for more details.

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