

Horizons could have you covered when bear emerges

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This is just a hunch, but the investing product of the year in 2007 could be a new exchange-traded fund that isn't actually available yet.

It's going to be called the Horizons BetaPro S&P/TSX 60 Bear Plus ETF and, once regulators approve it for sale, investors will have a nifty tool for profiting from a falling stock market. This isn't a prediction that 2007 will be a bad year for stocks, but rather an observation that after four years of above-average returns, something has got to give eventually. When it does, the people at Horizons BetaPro will have an ideal launching pad for their new ETF business.

The Canadian ETF market is dominated by Barclays Global Investors and its iShares franchise, which has close to \$14-billion in assets and has already squeezed out two competitors. State Street Global Advisors folded an ETF based on the Dow Jones Canada 40 index several years ago, and TD Asset Management mercy-killed its long-overlooked family of four ETFs this past March.

The first new Barclays challenger was Claymore Investments, which now has a family of five ETFs listed on the Toronto Stock Exchange. Horizons BetaPro is next, although it's hard to imagine the Barclays people worrying much about a pipsqueak competitor that is known only for a family of mutual funds that allows investors to

make bull-and-bear bets on various stock indexes and commodities, as well as the U.S. dollar.

Horizons BetaPro won't be a direct Barclays competitor, said Howard Atkinson, who recently left his job as head of public funds at Barclays to build HBP's exchange-traded-fund business. Rather, he sees his new firm as a niche player in the maturing ETF market.

Mr. Atkinson said the first phase of the ETF market was stock exchanges offering what used to be known as index participation units that allowed investors to capture the returns of an entire stock index in a single security. Phase Two was the entry of companies like Barclays, State Street and Vanguard, which have launched ETFs on virtually every global stock index of any significance.

"Phase Three of ETFs is niche players with niche indexes and specialty products," Mr. Atkinson said during a recent visit to Ottawa. "I think niche ETF providers are here to stay as long as you stick to your niche. If you went head to head against Barclays, you'd be crazy and we're not going to do that."

HBP will initially come to market with bull-and-bear plays on the S&P/TSX 60 index, which is a proxy for blue-chip Canada. Both are leveraged plays that give you 200 per cent of whatever the index does. If the S&P/TSX 60 index falls 2 per cent in a day, the bear fund would give you a gain of 4 per cent. The flip side: If the index rises 1 per cent, you lose 2 per cent.

The bear fund is most attractive because it offers a cheap, simple way for investors and advisers to hedge a portfolio of Canadian stocks and equity funds, and to profit in a down market. But this fund is not likely to find its way into the portfolios of middle-of-the-road, buy-and-hold investors who use ETFs.

James Steel, an Ottawa-based adviser who has used ETFs extensively for years, said he can see a case for the bear fund for those who believe the Canadian market is ripe for a fall. But he prefers to contain the risk of a market downturn in Canada the old-fashioned way -- through diversification.

"I would rather own a diversified portfolio with exposure to stocks not just from Canada but also the United States and internationally," said Mr. Steel, who is

executive vice-president with WDS Investment Management Ltd. "I know it's boring, but it works."

Leveraged ETFs like the two that Horizons BetaPro has in the works have already been launched in the U.S. market with some success. ProShare Advisors, the company that will manage the new HBP funds in Canada, has already attracted \$2-billion for the bull-and-bear funds it launched this summer, according to Mr. Atkinson.

The ProShares funds have a management expense ratio of 0.95 per cent, which compares with a projected 1 to 1.25 per cent for the HBP ETFs. That's flat-out expensive for an ETF, but with the 200-per-cent leverage these funds offer, you do get some extra zip for your invested dollars.

HBP's lineup of bull-and-bear mutual funds offers some hints about what future ETFs investors can expect. There are bull-and-bear takes on crude oil, gold, the U.S. dollar, the Nasdaq-100 index and Canadian bonds.

Mr. Atkinson said his firm plans to do some publicity for its new ETFs using surveys asking advisers whether they're bullish or bearish on the markets. Of course, nothing will sell the Horizons BetaPro S&P/TSX 60 Bear Plus ETF like the bear market we're going to get sooner or later.

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