Best Canadian ETFs:

Canadian ETFs vs Mutual Funds, Canadian Index Funds and More

Exchange Traded Funds
All You Need to Know about the Risks and Rewards

MAKING YOU A SUCCESSFUL INVESTOR

Best Canadian ETFs: Canadian ETFs vs Mutual funds, Canadian Index Funds and More

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The Birth of Exchange-Traded Funds

At the beginning of 2015 the global ETF industry had set a new record of $2.79 trillion assets held in 5,580 ETFs, listed on 62 exchanges in 49 countries. As of June 2015, Canadian listed ETFs held $87.4 billion in assets. The top 3 ETF providers as of the second quarter 2015 are iShares, SPDR, and Vanguard.

But how did exchange-traded funds (ETFs) develop into the widely traded investments they are today?

The forerunner to exchange-traded funds was indexing. Without indexing, ETFs would not exist. The word "index" refers to a sample of the market that is used to represent a statistical measure of the market as a whole.

Investment professionals have used indexing for years. Yet it wasn't until famed investor John Bogle created the first index mutual funds in 1975 that everyday investors had access to index-based investments.

Index mutual funds are a particular type of mutual fund in which the portfolio matches or tracks the components of a market index, like the S&P/TSX Composite Index or the Standard & Poor's 500 Index (S&P 500). Index fund managers will analyze and pick stocks trading on the index that have performed well within different industry groups like Consumer, Energy, Technology, and Financial.

Investors can then buy a single share of the index fund without having to buy separate stocks and pay separate transaction fees. This tracking of a market index led to the inception of the ETF.

The first ETF traded in 1989. It went under the name Index Participation Shares (IPS). IPS was an S&P 500 proxy that traded on the American Stock Exchange and the Philadelphia Stock Exchange. Because this product was so new and misunderstood, the Chicago Mercantile Exchange filed a lawsuit that successfully stopped the sale of IPS in the United States.

But in 1990, Toronto Index Participation Shares began trading on the Toronto exchange (then called the TSE). The fund, which tracked the TSE 35 blue chip index and later the TSE 100 index, became very popular. This popularity prompted U.S. markets to try again. By 1993, the United States Security and Exchange Commission allowed the sale of ETFs by US exchanges.

By the turn of the new century, ETFs had captured the attention of the investment market. Yet if it hadn't been for John Bogle's creation of index funds and the later success of Index Participation Shares on the Toronto exchange, the ETF might not have developed into the popular investment it is today.

What are ETFs?

Exchange traded funds (ETFs) are set up to mirror the performance of a stock market index or sub-index. They hold a more or less fixed selection of securities that represent the holdings that go into the calculation of the index or sub-index.

ETFs trade on stock exchanges, just like stocks. That's different from mutual funds, which you can only buy at the end of the day at a price that reflects the fund's value at the close of trading.

Prices of ETFs are quoted in newspaper stock tables and online. You pay brokerage commissions to buy and sell them, but their low management fees give them a cost advantage over most mutual funds.

As well, shares are only added or removed when the underlying index changes. As a result of this low turnover, you won't incur the regular capital gains taxes generated by the yearly distributions most conventional mutual funds pay out to unitholders.

Most investors would agree when we say that Exchange Traded Funds (ETFs) started out as the most benign investment innovation that has come along in our lifetimes.

However, as often happens after the successful launch of any new investment product, the financial industry soon came up with new, improved ETFs. The new models came with a wider variety of investor appeal, along with new wrinkles and extra costs.

The more complicated features there are in an exchange-traded fund (ETF), the more the investment firm can charge in fees and the more hidden risk you face when investing in ETFs.

However, unlike many other financial innovations, ETFs don't load you up with heavy management fees, or tie you down with high redemption charges if you decide to get out of them. Instead, they give you a low-cost, flexible, convenient alternative to mutual funds.

Because of this, we think ETFs have a place in your portfolio. If, as we advise, you keep it simple and stick to "plain vanilla" (see page 6).

They aim to provide the best of both worlds. Investors get the broad market exposure of a traditional mutual fund, plus the ability to trade at will with nominal fees. The best ETFs represent a low-cost, tax-efficient way for investors to make money in the long term.

Investors can buy ETFs via stock exchanges on margin or sell them short. The best ETFs offer well diversified, tax-efficient portfolios with exceptionally low management fees. Investors large and small use ETFs to build world-class diversified portfolios.

ETFs have added to their advantages over the last few years. That's because ETFs have evolved, and competition has increased. Still, you need to be very selective with your ETF holdings.

ETFs vs Mutual Funds

Mutual funds pool money collected from many investors and use the money to invest in securities, mainly stocks and bonds. The shareholders participate proportionally in the gain or loss of the fund.

Mutual funds can shift their portfolio allocations between stocks, bonds and cash in order to capitalize on perceived investment opportunities in any one of those classes.

Mutual funds let small investors access professionally managed, diversified portfolios that would be difficult for them to create on their own. The funds in turn charge investors management fees.

You can think of Exchange-Traded Funds (ETFs) as highly efficient mutual funds. The fees are low because investors don't pay for active management. Instead, ETFs aim to mimic the performance of a market index, by holding the same securities in the same proportions used to calculate the market index.

Here's why we prefer ETFs over mutual funds:

- ETFs are less expensive to hold in your portfolio. ETFs give you a low-cost way to invest in a narrow market segment. That's typically cheaper than investing in a mutual fund with a similar focus.

- Fees are as low as 0.10% a year for ETFs, whereas mutual funds can charge you 2% to 3% or higher on their fund. ETFs can save you a lot of money and boost your return if you are investing over time.

- ETFs trade on stock exchanges, just like stocks. That's different from mutual funds, which you can only buy at the end of the day at a price that reflects the fund's value at the close of trading.

- Prices of ETFs are quoted in newspaper stock tables and online. This makes them much more transparent than mutual funds.

- Shares are only added or removed when the underlying index changes. As a result of this low turnover, you won't incur the regular capital gains taxes generated by the yearly distributions most conventional mutual funds payout to unitholders.

For all of these reasons, we prefer ETFs to mutual funds. The best ETFs represent a more efficient and cost-effective investment.

Simple is better…especially with ETFs

Here's a good general rule to follow when choosing investments: Simple is better. The easier an investment is to explain and understand, the less likely it is to harbour hidden risks and costs that can only work against you. As the old investor saying goes, "Stick with plain vanilla."

For the investment industry, the rule works in reverse: The more complicated, the better. Each new feature provides a profit opportunity for the institution that sponsors the investment. It's particularly important to keep this in mind with ETFs.

These investments are like highly efficient mutual funds. Fees are low because investors don't pay for active management. Instead, ETFs aim to mimic the performance of a market index, by holding the same securities in the same proportions used to calculate the market index. As a liquidity feature, ETFs generally sell newly created units whenever their unit prices develop a premium over the value of the stocks they hold. They buy back units (in large blocks only, to keep costs low) when the unit price gets too far below the value of their holdings.

This simple arrangement yields only modest profit margins on "plain-vanilla" ETFs. The top ETF sponsors try to offset their low fees with high volume. Many ETFs have assets under management in the multi-billions.

However, adding more features (sometimes referred to as "wrinkles" or "bells & whistles") can make the ETF attractive to additional investors. Adding features also adds profit opportunities for the sponsoring institution.

For example, consider a typical ETF that gives you exposure to movements in an index of stock prices in an emerging market. This may appeal to investors who want to invest in that market. But conservative investors may hesitate to buy, because they worry about inflation in the emerging market. So the financial industry has come up with "hedged" ETFs.

The sales pitch is that you can profit from growth in the stock market of the emerging economy, but you avoid foreign-exchange risk because the ETF operator hedges against it. This conveniently overlooks the fact that hedging costs money.

Hedging costs will vary, depending on conditions in the foreign-exchange market, and on how an ETF carries out its hedging program. These fees can double or triple the typical 0.30% to 0.70% ETF management fee. Then too, hedging may only provide you with partial protection against foreign-exchange risk.

You'll need to dig deep to find out how much you pay for an ETF's hedging feature. But you can be sure that the placing of each new hedge provides a profit opportunity to the ETF sponsor.

Our view: simple is better. If you want to invest in something like emerging-economy stocks, limit your stake to a point where you can accept the associated foreign exchange risk. If you buy an ETF, choose a "plain vanilla" unhedged version. Or, to adapt yet another old investor saying, "If the foreign-exchange risk on your emerging-market investments keeps you awake at night, sell down to the sleeping point."

ETFs can make dumb moves easier

Most investors would agree when we say that ETFs started out as the most benign investment innovation that has come along in our lifetimes.

The problem is that ETFs work just as well in facilitating smart moves as dumb ones. And there are all sorts of dumb moves that ETFs can facilitate.

For example, if you get an urge to invest in oil stocks, or gold stocks, or Swedish stocks, or wind power stocks, or any of hundreds of other stock groups, you can act on that urge without doing any messy and time-consuming research on individual stocks.

In fact, you can act on your urge within minutes, since ETFs also trade on stock exchanges. You can buy or sell them at any time when the exchange is open. With conventional mutual funds, you can only buy or sell at the end of the day, at a price that reflects the value of the fund's holdings at the close of trading.

You can buy ETFs on margin, so your broker can provide instant financing for a portion of your purchase.

Many investors are seduced by the flexibility and low fees of ETFs, compared to conventional mutual funds. They overlook the fact that ETFs don't add any value to the underlying investment. Nor do they improve your market timing. They simply make it cheaper and more convenient to buy or sell.

Many brokers and portfolio managers have built a business around ETFs. Their sales literature focuses on how easy it is to invest in classes of investments. It's a great marketing gimmick, but it subverts the prime advantage of ETFs, which is low cost.

By the time the ETF specialists add their fees and commissions, their clients are paying the equivalent of actively managed MERs to buy what amounts to a hodge-podge of index funds. Liquidity and access to margin borrowing can come in handy, and low fees are better than high fees. But most successful investors owe much of their success to holding a diversified portfolio of well-established companies over a period of years if not decades.

Complicated, poorly-designed ETFs are more likely to lead you away from that path than help you follow it.

Newer ETFs vs original ETFs

The first ETFs had a simple goal: cutting fees for investors. Each new ETF aimed to copy the performance of a particular stock index (minus the costs of creating and running the ETF, of course). Most of the model indexes were well-known, widely followed collections of actively traded stocks.

These days, new ETFs aim to broaden investment opportunities for investors, and create new profit opportunities for the financial companies that sponsor them.

Instead of giving you a low-cost way to copy the results of a standard market index, new ETFs aim to mimic much narrower indices and higher-risk strategies.

They may give you a way to invest in a particular foreign stock market—coupled, in many cases, with an arrangement that hedges against movements in the foreign currency in which that foreign market carries on its trading.

Or they may give you a way to participate in a particular stock-market strategy.

New ETFs carry a somewhat higher management expense ratio (MER) than the old ones. Based solely on MERs, they're still cheaper to invest in than conventional mutual funds.
But MERs are just the start.

Many new ETFs need to delve into trading or derivatives of various sorts to accomplish their stated objectives (such as hedging against foreign currency movements). Rather than raising the ETF's MER, these added costs act as a drain on its capital. But the effect is the same. They act as a drag on the capital growth in an ETF, or speed the shrinkage in its value.

You might say these ETFs act as loss leaders for the industry. The institutions involved make little profit if any on the initial sale and yearly MER. They make up for it with profits from associated activities.

We don't mean to suggest that all new ETFs are aimed at fleecing investors. But we do believe investment quality varies just as widely with new ETFs as it does with new stock issues. In both cases, only a handful are worth holding, and only if you find their investment premise irresistible. Otherwise, you can find better investments.

Watch out for “theme funds”

Theme investing has a natural appeal. It simplifies things. Investors like it because they feel it can put their investment returns into overdrive. Some also feel it adds fringe benefits to their investing, by letting them support social or environmental objectives.

Brokers like it because it gives them a rationale to recommend a variety of stocks.

As an example, if a client thinks gold prices are headed up, a broker can think of all sorts of gold-themed investment opportunities including ETFs. They include established gold miners; junior gold companies that are working on a promising gold property; or penny golds that are outright speculations. Other possibilities are financial companies that sell gold-related merchandise like gold coins.

If the client supports environmental causes, the broker can propose investments with a “green theme”. They may include solar-power equipment makers; companies that claim their products are less harmful to the environment than competitors’ products; or companies that claim to operate with a high degree of environmental concern.

When you focus on theme investing, however, it’s easy to overlook the fundamentals. If you’re sure gold prices are headed up, for instance, why trouble yourself with tiresome matters like finances or geology?

Of course, many investing themes carry a grain of economic sense. Government spending deficits and money-supply growth of recent years will eventually lead to a rise in inflation. Gold may rise in response. The sun could one day become an economically attractive power source (though solar power generation now mainly runs on government subsidies). But it takes more than a grain of economic sense to turn a company into a profitable investment.

In the 1950s, some shoe stores kept a specialized x-ray machine on the sales floor. The ads on the store window said you could use the machine to check the fit on a new pair of shoes before buying them. Critics called it a gimmick to speed up shoe sales, and warned about the risk of needless exposure to x-rays.

Something like this happens today in the investment business.

For instance, finance industry marketers have discovered that ETFs are a potent selling tool. It can attract buyers for all sorts of theme investing schemes that would otherwise have little chance of success.

Stay away from this theme fund: Global X Social Media ETF

This particular ETF gives you an easy and low-cost way of investing in stocks associated with the “social media” investing theme. These stocks are now in the broker/media limelight. That’s not a particularly good time to buy. By the time the media has identified an investment theme like social media, and the investment industry has begun offering ETFs and other short cuts to investing in it, the best opportunities may have already come and gone.

Stocks that are in the broker/media limelight tend to expose you to extra risk. That’s because the favourable attention they get in the limelight pushes up investor expectations. When these stocks fail to live up to those heightened expectations, and that always happens eventually, stock prices can plunge.

Global X Social Media ETF isn’t in the limelight - the stocks it invests are. Some of the stocks it holds will eventually plunge when they fail to live up to investors’ heightened expectations.

GLOBAL X SOCIAL MEDIA ETF (Nasdaq symbol SOCL) invests in companies that provide social networking, file sharing and other web-based media applications.

This exchange traded fund holds 36 social media stocks. U.S. social media stocks make up 49% of assets. China is next with 28%; Japan, 12%; Russia, 7%; Ireland, 2%; Taiwan, 2%; and Germany, 1%.

The fund’s MER is 0.65%. It began trading as a new issue on November 14, 2011. Since then, it has been far more volatile than the Standard & Poor’s 500 market index, and has consistently underperformed the index. Since it began trading, the fund has gained around 40%. In the same time, the Standard & Poor’s 500 Index has gained around 62%.

The Global X Social Media ETF’s top 10 holdings are Facebook, Tencent Holdings, LinkedIn, Pandora Media, Alphabet, NetEase, Nexon, Sina Corp., Yahoo! and Dena Co. Ltd.

A number of the fund’s stocks are highly speculative. They could move higher in response to market sentiment, news releases and so on. But many of these shares are overvalued at today’s prices. They need great success to justify current stock prices, let alone move higher.

When the social media stock boom cools off, as it inevitably will, some of these stocks will drop to much lower levels.

We like some of the stocks the Global X Social Media ETF holds. The best example is Alphabet Inc., symbol GOOG (class C non-voting) and GOOGL (class A voting) on Nasdaq, a buy recommendation of our Wall Street Stock Forecaster newsletter. We now see Facebook and LinkedIn as holds for aggressive investors. We think a holding made up of equal parts of these three stocks may well outperform Global X, and you wouldn’t need to pay the 0.65% MER.

We don’t recommend the Global X Social Media ETF.

Another theme fund to avoid

DIREXION IBILLIONAIRE INDEX ETF (New York symbol IBLN) is designed to profit from copying the moves of billionaire investors, such as Warren Buffett, Carl Icahn, Daniel Loeb and David Tepper.

The ETF began trading on August 1, 2014. Its MER is 0.65%—lower than most mutual funds, but high for an ETF.

The Direxion iBillionaire Index ETF selects up to 10 billionaire investors from a pool of 50, based on their personal net worth, source of wealth, stock turnover and performance over time. It then selects stocks from their investment firms or hedge funds.

Each of the companies in the index is equally weighted (3.33% each) and rebalanced quarterly. That's because the ETF's managers aim to ensure that each stock's contribution to the fund's performance is identical.

The fund's managers select stocks by looking at Form 13F, a publicly available document that institutions, such as banks, hedge funds and investment firms, must file with the Securities and Exchange Commission (SEC). Form 13F discloses long positions, or stocks held with the intention of profiting if their prices go up.

The fund's holdings at last report were Apple, AbbVie, Allergan, Alphabet, Amgen, Baxter International, CONSOL Energy, Delta Airlines, Dow Chemical, eBay, Endo International, General Motors, Goodyear Tire & Rubber, HCA Holdings, Humana, MasterCard, Mohawk Industries, Monsanto, Microsoft, Micron Technology, Netflix, Priceline Group, Perrigo Co., Starwood Hotels, Thermo Fisher Scientific, Time Warner, Wallgreens Boots Alliance, Whirlpool, Williams Cos. and Yum! Brands.

Piggybacking on the investments of the rich is harder than it sounds, however, even with the help of Form 13F. For one thing, institutions have 45 days to file the form after each calendar quarter ends. By the time the fund starts buying, the billionaire buyer may have started to sell.

As well, 13Fs only disclose long holdings—stocks that the reporting institution owns. But hedge funds and billionaires generally sometimes offset their long positions with short sales. For example, a hedge fund may sell Hewlett-Packard short, to offset a "long" position on Microsoft. The hedger may think they are both over-priced, but that Hewlett will plunge sooner and farther than Microsoft. But form 13F only discloses the long position in Microsoft. This gives investors, including the iBillionaire ETF's managers, an incomplete and misleading picture.

An additional drawback of this continual rebalancing is that it costs money. The ETF has to absorb brokerage commissions and other transaction costs with each buy and each sale. As well, because it aims to keep each holding equal, it may add to its holdings of poor performers just because they've dropped in price, even though further declines may lie ahead. It also has to sell stocks that have gone up, perhaps missing out on some of these stocks' biggest gains.

This isn’t how billionaires get rich. But it is a drawback that’s common to all ETFs and other trading programs that follow a formula. The only thing guaranteed in a deal like this is that trading costs can offset any advantage you may derive from the ETF arrangement.

We don’t recommend the Direxion iBillionaire Index ETF.

Watch out for hidden costs

As often happens after the successful launch of any new investment product, the financial industry soon came up with new ETFs. The new models came with a wider variety of investor appeal, along with new wrinkles and extra costs.

The first ETFs had a simple goal: cutting fees for investors. Each new ETF aimed to copy the performance of a particular stock index (minus the costs of creating and running the ETF, of course). Most of the model indices were well-known, widely followed collections of actively traded stocks.

These days, ETFs aim to broaden investment opportunities for investors, and at the same time create new profit opportunities for the financial companies that sponsor them.

Instead of giving you a low-cost way to copy the results of a standard market index, many ETFs aim to mimic much narrower indices and higher-risk strategies. They may give you a way to invest in a particular foreign stock market—coupled, in many cases, with an arrangement that hedges against movements in the foreign currency in which that foreign market carries on its trading. Or they may give you a way to participate in a particular stock-market strategy.

Based solely on MERs, most ETFs are cheaper to invest in than conventional mutual funds. But MERs are just the start. Many ETFs need to delve into frequent trading or derivatives of various sorts to accomplish their stated objectives. Although they don't raise the ETF's MER, these added costs act as a drain on its capital. But the effect is the same. They act as a drag on the capital growth in an ETF, or speed the shrinkage in its value.

You might say these ETFs act as loss leaders for the industry. The institutions involved make little profit if any on the initial sale and yearly MER. They make up for it with profits from associated activities.

We don't mean to suggest that many ETFs are aimed at fleecing investors. But we do believe investment quality varies just as widely with ETFs as it does with new stock issues. In both cases, only a handful are worth holding, and only if you find their investment premise irresistible. Otherwise, you can find better investments.

Using ETFs in your Retirement Accounts

Your tax-free savings account (TFSA) allows you to earn investment income, including interest, dividends, and capital gains, tax-free.

Exchange traded funds (ETFs) can play a role in a TFSA. Using ETFs for growth within a TFSA is one popular long-term investing strategy.

TFSAs were first offered by the Canadian government in January 2009 with an annual contribution limit of $5,000. In 2013 the annual contribution limit increased to $5,500, in line with the initial promise to adjust limits with rising inflation. As of June 2015, the limit had been increased to $10,000. The new Liberal government lowered the annual contribution limit to $5,500—but without taking away any contribution room already accumulated.

That means that if you haven't contributed yet (and were 18 years or older in 2009) you can now contribute up to $46,500.

TFSAs are a bit different than registered retirement savings plans (RRSPs) because contributions to them are not tax-deductible. Withdrawals from a TFSA, however, are not taxed.

The best ETFs for TFSA growth will also provide you with a low-cost way to increase your exposure to larger portions of market sectors.

One general example is the iShares S&P/TSX 60 Index ETF (Toronto symbol XIU). The fund's units are made up of stocks that represent the S&P/TSX 60 Index, which consists of the 60 largest, most heavily traded stocks on the exchange.

Most of the stocks in the index are high-quality companies. You pay a commission to buy this fund (through a broker), but the fund's yearly expenses are just 0.17% of assets.

To sum up, here's why we recommend the use of ETFs in your TFSA:

1. ETFs diversify a portfolio. The limit is now $41,000 so you could build a diversified
2. portfolio of conservative, mostly dividend-paying stocks spread out across the five main
3. economic sectors (Manufacturing & Industry, Resources, Finance, Utilities and Consumer).
4. ETFs are fairly low risk. Holding higher-risk stocks in your TFSA is a poor investment
5. strategy because they come with a greater risk of loss. If you lose money in a TFSA, you lose both the money and the tax-deduction value of the loss.
6. ETFs are flexible. If funds are limited, you may need to choose between TFSA and RRSP contributions, but ETFs can be used for either.

RRSPs may be the better choice in years of high income since RRSP contributions are deductible from your taxable income. In years of low or no income — such as when you're in school, beginning your career or between jobs — TFSAs may be the better choice.

What you should know before buying ETFs

Investors use exchange-traded funds (ETFs) in a variety of ways. To make the best use ETFs, you should know both the advantages they offer, and some potential drawbacks.

Diversification is one of the most attractive features of ETFs. An investor could create an entire portfolio solely from a few well-diversified ETFs.

Most ETFs are low-cost investments. Typically ETFs are more tax-friendly and cheaper than other mutual funds or stocks. That does not mean that costs can't mount up.

Remember that ETFs trade on the exchange like stocks so that you pay a commission whenever you buy or sell. And of course you pay a management fee, which is usually lower than those you would pay for mutual funds, but can be higher for some newer ETFs (see page 8).

Here are several other important considerations.

Before buying ETFs you should know:

1. ETFs can be volatile, even with the diversification they offer.

2. How broad the base of the fund is, so you can determine its volatility. The broader the ETF, the less volatility it is likely to have.

3. The economic stability of countries when investing in international ETFs.

4. The liquidity of ETFs you invest in.

5. ETFs are subject to capital gains tax just like individual stocks if held outside a registered retirement account—and dividends distributed by foreign ETFs are not covered by the Canadian dividend tax credit.

6. That you can run up commissions with frequent trading.

As we've mentioned before, ETFs are set up to mirror the performance of a stock market index or sub-index. They hold a more-or-less fixed selection of securities that are chosen to represent the holdings that go into the calculation of the index or sub-index.

That way, if you want to invest in oil stocks, or gold stocks, or European stocks, or wind power stocks, or one of many other stock groups, you can do so without having to do extensive research on individual stocks.

On the following pages, we profile 11 ETFs that offer investors the greatest advantages and that we recommend for buying now.

11 top ETFs to buy now

Here are 11 ETFs we recommend as buys in our Canadian Wealth Advisor newsletter:

- **ISHARES S&P/TSX 60 INDEX FUND** (Toronto symbol XIU) is a good, low-fee way to buy the top stocks and income trusts on the Toronto Stock Exchange.

The units are made up of stocks that represent the S&P/TSX 60 Index, which consists of the 60 largest, most heavily traded stocks on the exchange. Most of the stocks in the index are high-quality companies. However, as the fund must ensure that it represents all sectors, it holds a few we don't recommend, such as Rogers Communications Inc. Expenses are just 0.18% of assets, and it yields 3.3%.

The index's top holdings are Royal Bank, TD Bank, Bank of Nova Scotia, CN Railway, Suncor Energy, Enbridge, Bank of Montreal, BCE, Manulife Financial, and CIBC.

iShares S&P/TSX 60 Index units are a buy for conservative investors.

- **ISHARES CANADIAN SELECT DIVIDEND INDEX FUND** (Toronto symbol XDV) holds 30 of the highest-yielding Canadian stocks. Its selections are based on dividend growth, yield and payout ratio. The weight of any one stock is limited to 10% of the ETF's assets. The fund's MER is 0.55%, and it yields 4.8%.

The fund's top holdings are CIBC, Bank of Montreal, Royal Bank, Bank of Nova Scotia, BCE, IGM Financial, Laurentian Bank of Canada, Rogers Communications and Manitoba Telecom.

iShares Dow Jones Canada Select Dividend Index Fund is a buy for conservative investors.

- **SPDR S&P 500 ETF** (New York symbol SPY) are commonly called "Spiders."

The ETF holds the stocks in the Standard & Poor's 500 Index, which consists of 500 major U.S. stocks that are chosen based on their market share, liquidity and industry group.

The index's 10 highest-weighted stocks are Apple, Microsoft, ExxonMobil, General Electric, Amazon.com, Johnson & Johnson, Wells Fargo, J.P. Morgan Chase, Facebook and Berkshire Hathaway.

The fund's expenses are just 0.10% of its assets. It yields 2.0%.

If you want exposure to the S&P 500 Index, the SPDR S&P 500 ETF is a buy for conservative investors.

- **SPDR DOW JONES INDUSTRIAL AVERAGE ETF** (New York symbol DIA) holds the 30 stocks that make up the Dow Jones Industrial Average.

The fund's top 10 holdings are Apple, IBM, Goldman Sachs, 3M, Home Depot, UnitedHealth Group, Walt Disney Co., Boeing, Nike and Travelers Companies.

The fund's expenses are 0.17% of its assets. It yields 2.2%.

SPDR Dow Jones Industrial Average ETF is a buy for conservative investors.

- **POWERSHARES QQQ ETF $108.00** (Nasdaq symbol QQQ) or "Qubes," hold the stocks that represent the Nasdaq 100 Index, which is made up of the 100 largest, most heavily traded stocks on the Nasdaq exchange.

The Nasdaq 100 Index contains firms from a number of major industries, including computer hardware and software, telecommunications, retail/wholesale trade and biotechnology. It does not contain financial companies. The shares' expenses are 0.20% of assets and it yields 1.2%.

The index's highest-weighted stocks are Apple, Microsoft, Alphabet, Cisco Systems, Intel, Amazon.com, Gilead Sciences, Comcast Corp. and Facebook.

PowerShares QQQ ETF is a buy for aggressive investors.

- **VANGUARD GROWTH ETF** (New York symbol VUG) aims to track the Center for Research in Security Prices (CRSP) U.S. Large Cap Growth Index, a broadly diversified index that mainly consists of large U.S. companies. The fund's MER is just 0.09% and it yields 1.3%.

The $50.3-billion Vanguard Growth ETF's top holdings are Apple, Alphabet, Gilead Sciences, Coca-Cola, Amazon.com, Facebook, Visa, Comcast, Home Depot and Walt Disney.

Vanguard Growth ETF is a buy for conservative investors.

- **VANGUARD FTSE EMERGING MARKETS ETF** (New York symbol VWO) aims to track the Financial Times Stock Exchange (FTSE) Emerging Index, which is made up of common stocks of companies in developing countries. The fund's MER is just 0.15%.

The Vanguard FTSE Emerging Markets ETF's top holdings include Taiwan Semiconductor (Taiwan: computer chips), Tencent Holdings (China: Internet), China Mobile, China Construction Bank, Naspers Ltd. (South Africa: media), Industrial & Commercial Bank of China, Bank of China, Hon Hai Precision Industry (Taiwan: electronics), Infosys (India: information technology) and Housing Development Finance (India: banking).

The $52.9-billion fund's breakdown by country is as follows: China, 27.2%; Taiwan, 14.4%; India, 13.3%; South Africa, 9.4%; Brazil, 7.2%; Mexico, 5.5%; Russia, 4.5%; Malaysia, 4.0%; Thailand, 2.7%; Indonesia, 2.2%; Philippines, 1.9%; Poland, 1.8%; Turkey, 1.6%; and others, 4.3%.

Vanguard FTSE Emerging Markets ETF is a buy for aggressive investors.

- **ISHARES MSCI GERMANY FUND** (New York symbol EWG) is an ETF that aims to track the MSCI Germany Index. This index aims to capture 85% of the German stock market's total market capitalization. The remaining 15% is unavailable for investment, partly because of limitations on foreign ownership.

The ETF's top holdings are Bayer (diversified chemicals), 9.6%; Daimler (automobiles), 7.3%; Siemens (engineering conglomerate), 7.1%; Allianz (insurance), 7.1%; SAP (software), 6.8%; BASF (chemicals), 6.6%; Deutsche Telekom, 5.1%; BMW AG, 3.1%; Deutsche Bank AG, 3.1%; Munich Reinsurance, 2.9%; Linde AG (industrial gases), 2.9%; Deutsche Post, 2.5%; and Fresenius (health care), 2.4%.

The fund was launched on March 12, 1996. It has an expense ratio of 0.48%.

Weak European markets have slowed the German economy's growth this year. Sanctions against Russia are also hurting German companies with a significant number of Russian customers.

However, the low euro remains a big plus for German exports, and the long-term outlook for the country's economy is sound.

iShares MSCI Germany Fund is a buy for conservative investors.

- **ISHARES MSCI AUSTRALIA INDEX FUND** (New York symbol EWA) is an ETF that holds the 71 largest Australian stocks. Its MER is 0.48%.

The fund's top holdings include Commonwealth Bank of Australia, 12.1%; Westpac Banking Corp., 9.3%; National Australia Bank, 6.9%; Australia and New Zealand Banking Group, 6.7%; BHP Billiton, 5.4%; CSL Ltd., 4.2%; Wesfarmers, 3.8%; Woolworths Ltd., 2.7%; Macquarie Group, 2.2%; and Telstra Corp., 2.1%.

Australia benefits from its stable banking and political systems and is rich in natural resources. Low commodity prices have hurt the country's economy, but its proximity to Asian markets with vast potential, including India and China, gives it strong long-term prospects.

iShares MSCI Australia Index Fund is a buy for conservative investors.

- **HORIZONS S&P/TSX 60 INDEX ETF** (Toronto symbol HXT) holds an index we see as a buy and it has a very low MER of 0.07%.

The ETF doesn't hold the actual stocks in the index, but rather financial instruments called total return swaps that replicate the index's return. Instead of paying dividends that are taxable each year, this ETF reinvests the value of the dividends and reflects them in the net asset value of the fund. You'll only pay tax on capital gains realized when you sell.

There is a credit risk with the counterparty that issues the total return swaps, but the risk is very low that a major Canadian bank or financial company would be unable to meet its obligations.

Horizons S&P/TSX 60 Index ETF is a worthwhile hold.

- **BMO DIVIDEND FUND** is a mutual fund that holds mostly highly-quality, large-capitalization Canadian and U.S. stocks.

The fund has 70.2% of its assets in Canadian stocks, 28.5% in the U.S. and 1.3% in other. It has a 1.80% MER.

BMO Dividend Fund's top stock holdings are: TD Bank, Bank of Nova Scotia, Royal Bank, Canadian National Railway, Enbridge, Starbucks, JP Morgan, Gildan Activewear, Brookfield Asset Management and Microsoft.

We think that for most investors exchange-traded funds (ETFs) offer better value with much lower fees than most mutual funds. So we feel that most fund investors should shift into ETFs wherever possible.

However, the BMO Dividend Fund is a worthwhile hold for most portfolios.

Conclusion

Smart conservative investing in ETFs gives you two big advantages. Your investments are safer when the market is down—and you're in a stronger position to profit when the markets move up. Pat McKeough's safety-first philosophy is simple and always effective. You can achieve surprisingly powerful results through both income and capital gains. And you never need to take big risks.

Our three-part investing program is our key investing principle, and it forms the core of all the advice you get in our newsletters and investment services, and on TSI Network.

These three safeguards will tend to limit your losses at the worst of times. But over long periods, they also let you profit nearly automatically.

1. **Invest mainly in well-established companies.**

   When the market goes into a lengthy downturn, these stocks generally keep paying their dividends, and they are among the first to recover when conditions improve.

2. **Spread your money out across the five main economic sectors (Manufacturing & Industry; Resources & Commodities; Consumer; Finance; and Utilities).**

   This helps you avoid excess exposure to any one segment of the market that is headed for trouble. Diversifying across the five sectors will also dampen your portfolio's volatility in the long term, without the shrinking in its potential that you'd get if you invest significantly in bonds yielding little more than 4%.

3. **Avoid or downplay stocks in the broker/media limelight.**

   That limelight tends to raise investor expectations to excessive levels. When companies fail to live up to expectations, these stocks can plunge. Remember, when expectations are excessive, occasional failure to live up to them is virtually guaranteed, in the long term if not in the short.

These three investing philosophy principles guide us in every portfolio we manage. Using these three value-investing principles will help protect your money during periods of market turbulence, and help you profit when the market rises.