CANADIAN

ETF Watch

WINTER 2025

CanadianETFWatch.com

Canada's ETF universe: WHERE THE MONEY GOES

- Canada's ETF Universe: Where The Money Goes
- How to Manage Portfolio Duration with Target Maturity Bond ETFs
- How First-time ETF A+® Awards Winners Excel

As the brisk winds of winter envelop the country, we are delighted to present the Winter 2025 edition of ***Canadian ETF Watch***. The Winter season is often a time for reflection, planning, and charting a course for the year ahead—principles that resonate deeply in the ever-evolving world of exchange-traded funds.

This edition highlights the dynamic growth of Canada's ETF industry and offers innovative strategies to help investors and advisors navigate the complexities of today's markets. Notably, Canada's ETF market has surpassed $450 billion in assets under management, with a 150% growth over the past five years—a testament to resilience and ingenuity in the face of market shifts.

In this Winter 2025 edition of ***Canadian ETF Watch***, we are proud to feature an array of insightful articles, including:

- **"Canada's ETF Universe: Where the Money Goes"**
  Brian Bridger, Senior Vice President, Analytics and Data, Fundata Canada Inc.
  An in-depth exploration of the ETF market's growth, trends, and diversification across equity, fixed-income, and alternative ETFs.
- **"How to Manage Portfolio Duration with Target Maturity Bond ETFs"**
  Stephen Hoffman, Managing Director of ETFs, RBC Global Asset Management Inc.
  Practical strategies for leveraging fixed-income ETFs to optimize portfolio yield and manage interest rate risks.
- **"How First-time ETF A+® Awards Winners Excel"**
  John Krisko, Vice President, Investment Analytics, Fundata Canada Inc.
  A celebration of innovative funds that balance risk and performance while excelling in the competitive ETF landscape.

As always, our mission is to empower you—our valued readers—with timely, actionable insights to support your investment journey. We hope this edition inspires you to embrace the opportunities and challenges of the year ahead with renewed vigor.

Thank you for being part of our ***Canadian ETF Watch*** community and we wish you a successful and prosperous winter season.

Sincerely,

Keith Costello
Global CEO,
Canadian Institute of Financial Planning
www.CIFP.ca

Ron Landry
Chair, The Canadian ETF Association
www.CETFA.ca

About *Canadian ETF Watch*

Through a dedicated website and quarterly issues, ***Canadian ETF Watch*** will speak to financial advisors, investors, managers and service providers to provide them with the latest information on ETFs in Canada. Canadian-based ETF markets continue to grow, which presents numerous marketing and promotional opportunities. Fund companies benefit from being featured in Canadian ETF Watch as their company name and solutions are distributed to our audience who are dedicated & targeted to ETFs.

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1 Source NBF ETF Research. Bloomberg Data as of March 31, 2024.

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Canadian ETF Watch is published quarterly by
Radius Financial Education & **Canadian ETF Association (CETFA).**
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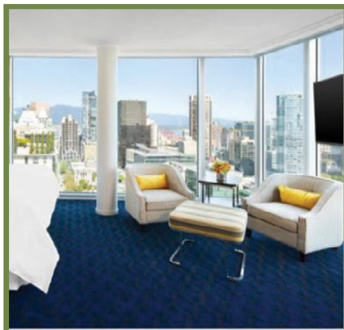

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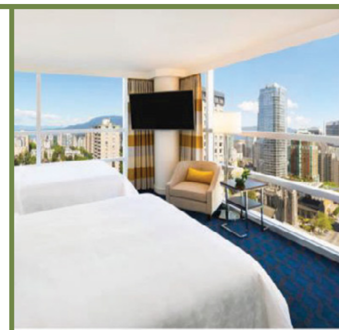

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Canada’s ETF Universe: Where The Money Goes

Investing is a numbers game. Prices, performance metrics, statistics are the daily meat and potatoes of investors, analysts, and managers.

Brian Bridger,
Senior Vice President,
Analytics and Data
Fundata Canada Inc.

But numbers can tell us a lot not just about investment performance of a single security, but also the state of entire markets. The Canadian exchange-traded fund (ETF) market is a case in point.

In fact, the world’s first ETF was created in Canada in 1990. From that modest beginning, the Canadian ETF market today has grown to 1,536 funds. And assets under management are north of $450 billion, a 150% increase over the past five years, or a 20% compounded annual growth rate.

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Equity-based ETFs dominate

The largest percentage of Canadian ETFs are equity-based, at 62% (953 funds). Fixed Income funds form the next largest category at 26%. A much smaller portion of the market share is claimed by Commodities at 5%, Balanced at 4%, and finally Cash, which includes money market and high interest savings funds, making up 2%.

Equity ETFs include all funds that primarily invest in equity securities as well as derivatives with exposure to equity markets. These exclude alternative funds such as long-short equity strategies. In the equity space, factor-based strategies account for the largest group of funds, at close to a 33% share. And while factors can include things like growth, momentum, and quality, the largest factor strategy belongs to dividend funds, which make up over 37%. Another popular factor is low volatility (15%). At the other end of the spectrum there are two ETFs that are based on gender diversity metrics.

Sector-based ETFs account for 28% of the equity universe, with technology funds comprising around 22% of this category, while financials make up 19%. Broad market ETFs, which can be either index-based or actively managed, make up 33% of the equity funds, with U.S.-focused funds accounting for 36% and Canadian funds at just a third of that, at only 13%.

Some of the more niche equity ETFs include a handful of options-based funds that include put-writing strategies. There are also a growing number of ETFs that track a single U.S.-listed stock, such as Amazon or NVIDIA.

From a risk perspective, the majority of equity ETFs (62%) are rated medium risk, while 14% are rated high risk. Just 4 equity ETF is rated low risk.

Another way to slice up the equity category is by management style. Close to half (48%) of equity ETFs are still index funds (often called “passive” funds) whose objective is to track an index such as the S&P/TSX Composite or the Nasdaq Composite, with no investment decisions made by a manager. Actively-managed funds, which include ETFs where the manager makes the investment decisions, make up 30%. Rules-based funds, where prescribed rules are used to make investment decisions, make up 11% of management styles. Enhanced index ETFs, which include ETFs that track an index and overlay a strategy (primarily using covered calls) to limit downside, produce additional income, etc., comprise 10%.

Fixed-income ETFs invest primarily in investment-grade government and corporate bonds, as well as emerging market debt, high-yield bonds, and preferred shares. Geographically, Canadian-focused funds make up 40% of this category, while U.S. funds take a 27% share, and global funds at 25%. In the fixed-income category, 62% of funds are actively managed, while 35% are index based.

In recent years, non-conventional investment strategies (e.g., short-selling and other forms of leverage, derivative contracts, and so on) dubbed “Alternative” investments, have become increasingly popular with money managers and more sophisticated investors. Accordingly, financial markets, being endlessly innovative, introduced Liquid Alternative funds to make such strategies more easily available to investors. These funds now make up 12% of all Canadian ETFs. Within the category, cryptocurrency funds make up 20%, while 16% are funds using Passive/Inverse Leveraged strategies.

From a currency perspective, 86% of all ETFs are denominated in Canadian dollars with the remainder denominated in U.S. dollars.

Responsible Investment (RI) funds, as defined by the Canadian Investment Funds Standards Committee (CIFSC), make up over 7% of all ETFs. The majority of these are Equity funds, at 73%, while Fixed Income funds account for 21%.

Fees and performance of ETFs

Looking at fees, Equity ETFs have an average management expense ratio (MER) of 0.66%, and Fixed Income funds average 0.49%. Active Equity funds average 0.91%, index-based funds average 0.44%, and rules-based funds average 0.63%. In the Fixed Income space, index ETFs have an average MER of 0.25% while active funds average 0.68%. Alternative funds have the highest average MER, at 1.61%. When comparing ETF fees with mutual funds, it is important to keep in mind that MERs do not include any brokerage fees that can be associated with buying and selling ETFs.

So what does all of this mean for performance? Year to date (YTD) to the end of November, Equity ETFs on average, have gained 21.5%. Fixed Income funds are up 3.9%, and Cash funds made 6.7%. Of the Equity funds, U.S.-focused funds lead the way at 26.6% YTD, followed by Global funds at 21.2%, and then Canadian at 20.8%. Over the past three years, U.S. funds were still the top performers, with an average annual compounded rate of return of 9.2%, followed by Canadian funds at 8.5% and then Global funds at 6.2%. Of the three groups, Canadian funds were the least volatile, with a standard deviation (SD) of 17.2%, slightly lower than the U.S. and Global funds.

For Global and U.S.-focused equity funds, rules based strategies outperformed over the past three years, gaining 10.8% and 9.9%, respectively. For Canadian focused equity funds, Index strategies led the way with a return of 8.9%. Across all three regions, active strategies were by far the least volatile, with an average standard deviation of 14.8% compared with 18.5% for the other management styles.

Brian Bridger, CFA, FRM, is Senior Vice President, Analytics and Data, at Fundata Canada Inc. and is a member of the Canadian Investment Funds Standards Committee (CIFSC).

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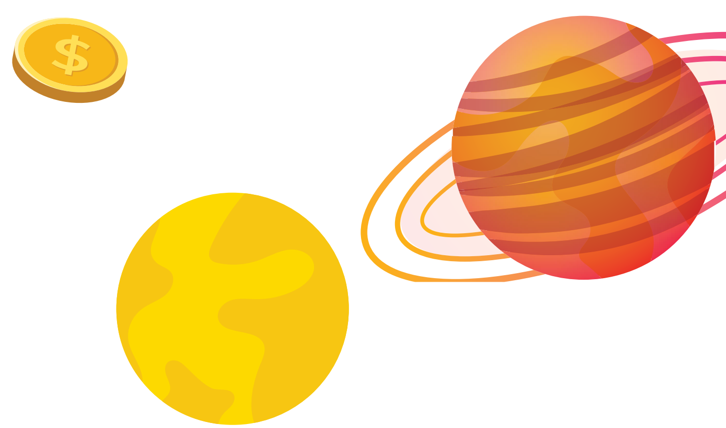

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How to Manage Portfolio Duration with Target Maturity Bond ETFs

Stephen Hoffman,
Managing Director of ETFs, RBC Global Asset Management Inc.

Investors have been pouring back into the fixed income market thanks to the rise in interest rates over the past two years. Now, with yields beginning to ease and further central bank cuts on the horizon, investors are facing a new challenge.

How can they find a flexible, easy way to capture higher yields while also managing interest rate risk within their portfolios? One way advisors can help is by offering a solution that allows their investor clients to tailor duration.

RBC Global Asset Management

Target maturity bond exchange-traded funds (ETFs) hold bonds that mature in the same calendar year as the ETF itself. With that, advisors can more precisely manage overall portfolio duration, which is beneficial in a declining rate environment. These ETFs also offer steady income much like an individual bond, as well as access to a diversified basket of bonds, all in one simple transaction.

"Target maturity bond ETFs allow investors to easily manage their fixed income exposure, duration and maturities to meet their risk and timing needs," says Stephen Hoffman, managing director of ETFs at RBC Global Asset Management Inc. (RBC GAM) in Toronto.

These products have attracted significant asset flows because of their unique characteristics – they mature like a bond, trade like a stock and are diversified like a fund. RBC GAM's suite of target maturity bond ETFs, with more than $3.5-billion in assets under management, makes them an industry leader.

Mr. Hoffman refers to target maturity bond ETFs as a hybrid fixed income strategy offering the benefits of both individual bonds and traditional bond ETFs.

For example, investors purchasing RBC Target 2026 Canadian Corporate Bond Index ETF (ticker RQO) know the fund's underlying bond holdings will all mature in 2026. This gives them a clear view regarding the yield to maturity they can expect to receive the moment they purchase the ETF, which is markedly different from traditional fixed income ETFs.

"There has always been a challenging element associated with bond ETFs, in that they don't have a set maturity," says Yves Rebetez, an ETF expert and co-founder of Global Allocators, an industry consulting firm in Calgary. "They keep on providing exposure to a broad bond index, whereby maturing bonds disappear, and new bonds are added."

Traditional bond ETFs maintain a fairly consistent duration, which does not change much over time. That's true whether you own the ETFs for a year or a decade, Mr. Hoffman says. "In contrast, a target maturity bond ETF's duration naturally decreases over time as you get closer to maturity. That gives you a lot more control over your exposure."

The fund structure also offers obvious advantages over purchasing individual bonds. Besides the diversification of having exposure to dozens of bonds, these ETFs offer intraday liquidity with tighter bid/ask spreads. "That's a huge advantage, helping investors to save money," Mr. Hoffman says.

He notes that target maturity bond ETFs aren't a one-ticket solution for fixed income in a portfolio. Rather, they complement other fixed income holdings and are particularly useful for retirees or other investors with income needs for a specific year.

When a target maturity bond ETF matures, investors see their capital returned to them. This clarity makes executing bond strategies in portfolios "cleaner" for many advisors, Mr. Rebetez says, which is useful for strategies like bond laddering.

"Typically, a five-year bond ladder requires owning 15 to 20 bonds to be well diversified, which is a lot to manage for many clients," Mr. Hoffman notes.

Using a target maturity bond ETF for each rung involves much less time, effort and cost, while providing greater diversification.

Compared to using guaranteed investment certificates in ladders, for example, target maturity bond ETFs provide advisors with greater liquidity.

Despite the utility of these ETFs, many investors are still unfamiliar with them. That's why RBC GAM, which was first to market with target maturity bond ETFs in 2011, works closely with advisors and other investors to boost knowledge around how they can be used.

"We have products that offer Canadian government or corporate bond exposures with maturities ranging from 2025 to 2030. And we recently launched U.S. corporate target maturity bond ETFs with target maturities from 2025 to 2030, so there's a broad spectrum of offerings," Mr. Hoffman says.

"We have 13 years of experience managing and maturing these products," he adds, "and so we can help investors understand how these ETFs behave, especially as they mature.

Content produced by: Globe Content Studio

Published September 16, 2024

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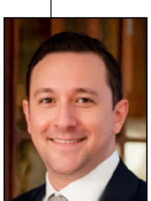
How First-time ETF A+® Awards Winners Excel

The past year continued to be marked by global challenges, ranging from regional conflicts to political strife, alongside significant political changes closer to home on both sides of the border.



John Krisko,
Manager,
Analytics and Data
Fundata Canada Inc.

Despite these challenges, the S&P/TSX Composite rose by 18% and the S&P 500 gained 23% through November 30, 2024. These impressive returns reflect the strong performance of markets at large with all but one Canadian Investment Funds Standards Committee (CIFSC) category generating significant positive returns.

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While broad returns have been high across the board, certain funds distinguish themselves by delivering consistent returns while limiting price volatility. Greater price stability reduces investment risk by providing more predictability in the value of an investment. Risk-adjusted returns take this into account and reflect the amount of risk it took to generate a given return. These returns form the basis of the annual FundGrade A+® Awards.

The annual FundGrade A+ Awards hosted by Fundata Canada recognize and acknowledge excellence in the Canadian investment fund industry through the year. The award is based on strictly objective criteria and looks at funds' risk-adjusted returns from 2 through 10 years. Funds are assigned a monthly grade, and those that consistently earn a high grade throughout the year are awarded an A+ rating.

Two ETFs led their respective categories among the contenders for the 2024 A+ Awards.

New category, new winner

Middlefield Sustainable Global Dividend ETF (TSX: MDIV) is not only in line to win its first A+ Award but it would also do so in one of two new CIFSC categories launched this year: Global Dividend & Income Equity. Along with a U.S. counterpart, the CIFSC created these categories as peers to the Canadian Dividend & Income Equity category, reflecting the growing popularity of dividend-focused investments outside of Canada.

With a dividend yield of nearly 4% and a 1-year return of 44% through November 30, MDIV has one of the highest returns of all potential A+ funds and a dividend yield nearly double its category benchmark. This performance is no exception as the fund has consistently earned high returns throughout the 10-year period included in the A+ calculation, culminating with a 10-year Sharpe ratio of 0.79 on an 11.4% annual return.

MDIV also follows a responsible investment mandate and is flagged by the CIFSC Responsible Investment Framework as ESG Best in Class, ESG Exclusions, and ESG Related Engagement and Stewardship Activities. The fund specifically screens for companies that exhibit above-average ESG characteristics, while excluding companies in "ethically-contentious industries" (such as tobacco and weapons). In addition, the manager engages with the companies they invest in to advance ESG initiatives through meetings and proxy voting.

Classic category, distinguished performance

Another strong first-time contender for a FundGrade A+ Award in the Canadian Equity category is First Trust Canadian Capital Strength ETF (TSX: FST). The fund delivered a 1-year return of nearly 35% through November, coupled with a low standard deviation of 2.44%. Its 1-year Sharpe ratio of 0.89 has significantly outperformed the category average Sharpe ratio of 0.65, driven largely by the category's much higher volatility of 8.6%.

What is behind FST's consistent outperformance? The fund employs a "bottom-up, multi-step quantitative and fundamental stock selection strategy" that aims to identify what manager First Trust Portfolios calls "capital strength issuers." These companies are characterized by four key factors: well-capitalized balance sheets; the ability to grow earnings; high liquidity; and a history of profit growth and financial strength. These factors have led the fund to an annual return of 12.4% over the past five years.

1-year return, Standard Deviation, and Sharpe ratio for A+ Award contenders vs category average

Fund and Category	Return (%)	Std Dev (%)	Sharpe Ratio
Middlefield Sustainable & Income Equity	44.23	2.15	1.28
Global Dividend & Income Equity	23.39	6.90	0.73
First Trust Canadian Capital Strength ETF (FST)	34.81	2.44	0.89
Canadian Equity	25.99	8.56	0.65

Source: Fundata Canada Inc. As of Nov. 30, 2024

John Krisko, CFA, BBA, is Vice President, Investment Analytics at Fundata Canada Inc. and is Vice Chair of the Canadian Investment Funds Standards Committee (CIFSC).

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