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CANADIAN ETF Watch

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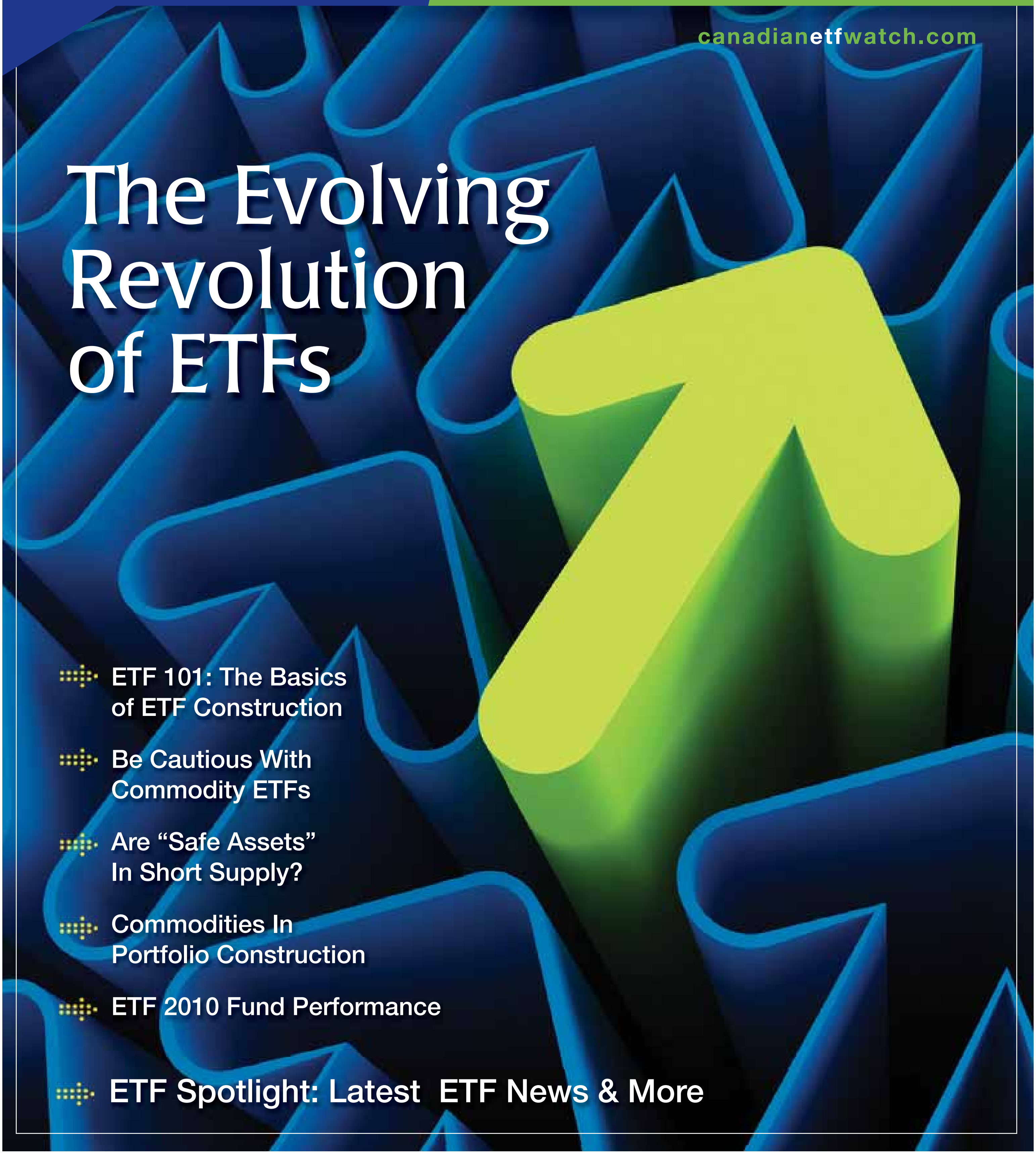

The Evolving Revolution of ETFs

- ETF 101: The Basics of ETF Construction
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The ETF industry continues to swell, becoming an undeniable force in the financial universe.

The global ETF and ETP industry combined, had 3,649 products with 7,583 listings, assets of USD1,542.7bn from 174 providers on 52 exchanges around the world according to Blackrock's latest ETF Landscape report. This compares to 2,721 products with 4,919 listings, assets of USD1,152.2bn from 139 providers on 43 exchanges, at the end of February 2010.

The ETF industry continues to swell, becoming an undeniable force in the financial universe. The growth of the ETF industry has been a positive development for investors, but there are always two sides to the coin when it comes to increased publicity. In 2010, more ETF critics emerged and attacks on the industry began to make headlines. Consider this: The ETF universe is still dwarfed by the mutual fund industry, but the tides are starting to change. ETFs aimed at longer-term investors continue to chip away at mutual fund assets, and transparency continues to be a huge factor in the post-crisis U.S. economy.

In 2011, the ETF industry will continue to expand along with the number of critics who are looking to cast doubt. In the year ahead, investor education will be more important than ever.

Our objective here at **Canadian ETF Watch** is to help Canada's ETF investors, advisors, providers and managers tell the whole story with informed commentary and analysis from leading ETF professionals themselves. By providing an objective platform, **Canadian ETF Watch** serves both investor and funds alike, bringing the two together in an exchange of news and views with the clear goal of providing more comprehensive and informed perspectives.

ETFs are not new. But their continuing growth and success makes them a significant element in contemporary portfolio construction. Canadian-based ETFs are in the midst of rapid expansion, a trend that shows no signs of slowing down. ETF Managers have a story to tell... advisors and investors need to get the whole story. **Canadian ETF Watch** is the place where both sides meet.

Speaking of education, we look forward to seeing you at our second annual **Exchange Traded Forum** where we will once again focus on educating advisors and investors on all exchange traded products. Based on the feedback from last year's forum, we have added ETF workshops at both the beginner and advanced levels. We will also spend time looking "under the hood" at product construction and choosing the right strategy to fit your clients needs. So please mark **May 10 & 11** on your calendar for our Toronto conference and for all our western Canada subscribers, we will be hosting our 1st annual Exchange Traded Forum's in **Calgary** on **June 20th** and **Vancouver** on **June 22nd**. Complete conference details can be found at **www.exchangetradedforum.com**

Tony Sanfelice, President
Radius Financial Education

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Editor
Terry Krotowski

Contributing Writers
John Gabriel, Alfred Lee, Oliver McMahon, Tyler Mordy, Mark Yamada

Research
Terry Krotowski

Sales Director
Judy Street

Art Direction
Vic Finucci

Online Developer
Ferenc Schneman

Contact Information
Canadian ETF Watch
20 Toronto St., Suite 820, Toronto, Ontario M5C 2B8
tel: 416.306.0151 ext. 2225

Editorial, Media & Advertising
Terry Krotowski krotowski@radiusfinancialeducation.com

Subscriptions
subscription@canadianetfwatch.com

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Types of ETFs

There are a variety of ***Exchange Traded Funds (ETFs)*** *that provide investors an opportunity to develop a diversified investment portfolio. ETF sponsors are constantly adding to the types of ETFs available, providing investors with more choice. Many ETFs track the performance of an underlying index or benchmark. The underlying index or benchmark may be broad, or sector-specific, or be linked to commodities or currencies. ETFs have evolved, however, to include those that do not passively track an underlying index or benchmark.*

ETFs can be grouped into different categories, which may include:

Index ETFs

ETFs that use an index tracking approach generally follow a pre-selected index, called a benchmark, and the return on the ETF will closely correlate with that of the underlying index. Index ETFs follow a variety of indices, including the broad market (both Canadian and international), sectors such as infrastructure or health care, and commodities (including natural gas, oil and gold), as well as indices that offer exposure to dividends or fixed income. The weightings used in the underlying index could be based on market capitalization of the constituents or on fundamental factors such as financial criteria. Index ETFs may also follow indices that adhere to a certain investment style, such as value or growth.

Inverse and Leveraged ETFs

Inverse ETFs are designed to seek daily investment results that correspond to the inverse daily performance of their underlying index or benchmark. To meet their investment objectives, inverse ETFs use a variety of derivatives such as futures contracts and index swaps to reproduce a daily result that is the opposite of the underlying index or benchmark; so, when the index or benchmark goes down in value on a given day, the inverse ETF will correspondingly go up in value for that given day. Conversely, when the index or benchmark goes up in value, the inverse ETF will correspondingly go down in value. Investing in these ETFs is similar to holding short positions, or using a combination of advanced investment strategies to profit from declining prices.

Leveraged ETFs are designed to seek daily investment results to provide a multiple of the daily performance return of an underlying index or benchmark (for example, 200% the return). They are not intended to provide that same multiple of the return over the mid or long term. Investors should be aware that, while leveraged ETFs typically achieve their stated objective of a multiple of the daily performance of an underlying index on a daily basis, their returns can vary considerably from that stated objective if held for a period longer than one day. Note that some leveraged ETFs are also inverse, in that they track the opposite of the return of an underlying benchmark.

To meet their investment objectives, leveraged ETFs use a variety of derivatives such as futures contracts and index swaps to provide a multiple of the market exposure of the stocks in the fund. Leveraging increases the risk of the investment in such an ETF, in that losses will be magnified by that same multiple.

Inverse and leveraged ETFs are generally intended for use in daily or short-term trading strategies, and are not intended for investors who are looking to hold positions in a security beyond the short-term. Over time, a leveraged fund can drift from its benchmark due to the effects of compounding, especially during periods of market volatility. Therefore, the return on these ETFs for periods longer than a single day will not correlate with the return of the underlying benchmark. Accordingly, significantly more risk is involved in these types of ETFs than in index ETFs.

It is important that investors clearly understand the nature and risks of any ETF prior to investing.

Commodity ETFs

Commodity ETFs provide exposure to commodities such as energy (e.g., natural gas or oil), precious metals (e.g., gold, silver or platinum), or livestock and grains, either by (i) holding the physical commodity directly, (ii) tracking the performance of the spot market price through physical forward contracts, or (iii) investing in or tracking the performance of commodity futures contracts. ETFs that hold the physical commodity provide exposure to the spot price of the commodity without the trouble of storing the commodity. ETFs that hold futures provide exposure to futures without the trouble of rolling them over. Most commodity indices are futures price indices, reflecting a change in the price of commodity futures, not in the commodity price.

Currency ETFs

Currency ETFs provide exposure to currencies and can also hold either the actual currency or futures contracts. Some are designed to be long or short on one currency against others; some are designed to hold a mix of long and short futures positions among several currencies.

Actively Managed ETFs

Index ETFs are generally designed around a passive strategy and therefore typically have lower management fees. Some ETF providers offer actively managed ETFs that operate more closely to the concept of a mutual fund. These ETFs have an active manager making investment decisions, often with the objective of outperforming rather than tracking a particular benchmark index, but usually with lower management fees than a traditional mutual fund.

Exchange Traded Notes (ETNs)

Exchange traded notes are debt obligations of the issuer and trade like ETFs. They do not guarantee any return of principal at maturity and do not pay any interest during their term. While they exhibit no tracking error in that their return at maturity is linked to the return of the underlying index (minus expenses), they do exhibit credit risk linked to the issuer. ETNs offer long and short or inverse exposure to commodities and currencies as well as leveraged exposure.

Source: tmxmoney.com

The Evolving Revolution of ETFs

What's next and why.

Mark Yamada
President & CEO,
PUR Investing Inc.

Once an opaque pastime for the rich, investing has been hidden behind obscure terminology, highly paid advisors, and arcane documents, like the mutual fund prospectus. The digital age is changing all that. ETFs are weapons in the movement to emancipate individual investors.

The explosive growth of exchange traded funds (ETFs) has been both exciting and bewildering. Retail investors, excited by broad access to timely, low-cost, tax efficient and diversified exposure to capital markets are also bewildered by the scope, breadth and number of products – 224 in Canada, 3,500 globally and 500 ETFs in registration with the Securities and Exchange Commission (March 2011). Sorting, selecting and constructing portfolios are new and growing challenges for investors. Nevertheless, ETFs have provided only the second significant advance for individual investors since the popularization of the mutual fund in the 1990s (the first being the introduction of the index mutual fund).

Mutual fund companies must also be excited and bewildered. Traditionally marketers and distributors of investment products, banks and fund companies are reassessing their business models. Scale has always been important but it is critical today with compliance expanding and margins contracting. Although the mutual fund continues to dominate retail investing, better-informed investors recognize that costs matter and that in an interconnected world, transparency and access to pricing more than once a day should be fundamental.

PUR INVESTING INC.

ETFs, because they are listed directly on stock exchanges without having to be "approved" by a sales entity, provide a distribution "end run" around the established axis of bank and fund company control, and give buying choice directly to individual investors. Furthermore, the hype around "star" managers and persistent marketing of past performance has worn thin. It is not exactly breaking news that past performance is no indication of future performance.

Sophisticated investors have been using ETFs for over a decade, but the broad public is catching on, albeit slowly. Early adopters of ETFs have been CEOs, senior executives, sophisticated high net worth investors, and investment professional themselves. However, innovation is still driven by professional money managers motivated by increasingly knowledgeable institutional clients. Individual investors can exploit these trends and ETFs enable them.

Democratizing Diversification

The principle of diversification is not new. Natural selection and evolution itself may have been the first practical implementation of diversification as a means for the species to survive. Harry Markowitz put form around the substance of portfolio diversification in (Modern) Portfolio Theory (1952). Retail and institutional investors already knew not to put all their eggs in one basket but it wasn't until the 1970's that index or passive investing became pervasive among large institutional portfolios about ten years after the introduction of the Capital Asset Pricing Model (CAPM) suggested a distinction between systematic non-diversifiable or market risk, β, and unsystematic diversifiable idiosyncratic or asset specific risk, α. The idea of combining a low cost passive core portfolio using index strategies to capture broad market (β) returns and using satellite portfolios to generate excess (α) returns has been accepted institutional practice for 30 years. Importantly, passive investing, once the domain of the largest institutions and pension funds is becoming "mainstream".

Investment professionals were the first to embrace exchange traded funds (ETFs) when the Toronto Stock Exchange introduced Toronto Index Participation Shares (TIPS) in 1990. Replicating the TSE 35 Index (predecessor of the S&P/TSX 60 Index), institutional managers found they could rapidly deploy cash in a diversified manner using TIPS. Individual investors gained their first access to instant transparent diversification through an exchange as a result.

Diversified Canadian Equity – ranked by diversification and cost	Symbol	MER
iShares S&P/TSX Capped Composite	XIC	0.25%
BMO Dow Jones Canada Titans	ZCN	0.16%
Horizon BetaPro S&P/TSX 60	HXT	0.07%
iShares S&P/TSX 60 Index	XIU	0.17%

International Diversification

Thirty years ago, international equities were considered "alternative" asset classes. Access to markets and diversification within them were barriers. Not so today. ETFs offer access to a growing array of international markets. The emerging markets are an area of particular interest to professional investors. As a consequence, more granular choices are available to all.

International or Global Equity - ranked by diversification and cost	Symbol	MER
iShares MSCI World Index	XWD	0.45%
iShares MSCI EAFE	XIN	0.50%
BMO International Equity Hedged to CAD	ZDM	0.49%
Claymore International Fundamental Index		
(hedged and non-hedged)	CIE	0.68%
Emerging Markets Equity – ranked by diversification and cost		
iShares MSCI Emerging Markets Equity Index	XEM	0.82%
BMO International Equity Hedged to CAD	ZEM	0.54%
Claymore Broad Emerging Markets	CWO	0.65%
Specific Emerging Markets Equity - ranked by diversification and cost		
Claymore China	CHI	0.70%
Claymore BRIC	CBQ	0.64%
BMO China Equity Hedged to CAD	ZCH	0.71%
iShares MSCI Brazil Index	XBZ	0.75%
iShares China Index Index	XCH	0.85%
iShares CNX Nifty India Index	XID	0.98%
iShares MSCI Latin America 40 Index	XLA	0.65%
BMO India Equity Hedged to CAD	ZID	0.71%

The Three Factor Model and the Style Box

Institutional managers have found CAPM a useful but imprecise tool. The Fama-French three factor model added style (value/growth) and size (small cap/large cap) to market risk finding that, for U.S. equity markets over time, value outperformed growth and small capitalization stocks outperformed large capitalization stocks. These simple ideas provided the basis for the Morningstar Style Box™ of money management categorization (1992) and contributed to the popularization of mutual funds over the past two decades. ETFs are available that address all three factor approaches.

Value Canadian Equity – ranked by diversification and cost	Symbol	MER
Claymore Canadian Fundamental Index	CRQ	0.69%
iShares Dow Jones Canada Select Value	XIC	0.25%
Horizon AlphaPro North American Value	HAV	0.70%
Growth Canadian Equity – ranked by diversification and cost	**Symbol**	**MER**
iShares Dow Jones Canada Select Growth	XCG	0.50%

Small Cap Canadian Equity – ranked by diversification and cost	Symbol	MER
iShares S&P/TSX SmallCap	XCS	0.55%
iShares S&P/TSX Completion Index	XMD	0.55%

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Sectors and Countries

If three factors are good, more must be better. Breaking market risk into more component factors can be a comprehensive way to control components of risk. The simplest example is the aready-pervasive practice of isolating sectors and industries domestically and globally. Canadian sector ETFs are available for energy, financials, information technology, materials and REITs from iShares with choice in most offered collectively by BMO, Claymore and Horizon BetaPro. Global sectors include agriculture, real estate, and water offered by Claymore with choice in metals and infrastructure offered by BMO.

For U.S. markets, BMO offers banks, healthcare and NASDAQ ETFs. Investors with access to U.S. markets get an even broader palette of ETFs in every sector imaginable. On the fixed income side, there is a growing list of sector, quality, and term choices with international and inflation protection included. Commodities and income choices are also pervasive.

What's Next and Why

Investors who experienced the financial crisis and market meltdown in 2009 know that there were few places to hide from the twin forces of volatility and a liquidity vacuum. At one end of the spectrum, broad diversification did not save portfolios nor did stock picking at the other.

Expect more creative approaches towards diversification. Income generation is a popular one at the moment.

Income – ranked by diversification and cost	Symbol	MER
iShares Diversified Monthly Income	XMI	0.55%
BMO Monthly Income	ZMI	0.55%
Claymore Canadian Financial Monthly Income	FIE	0.65%
Claymore S&P/TSX CDN Preferred Share	CPD	0.45%
iShares S&P/TSX Preferred Stock Index Hedged to CAD	XPF	0.45%

Alternative approaches will also start to appear in Canada that replicate hedge fund strategies. BMO's Covered Call Canadian Banks (ZWB 0.65%) and Horizons AlphaPro S&P/TSX 60 130/30 Index (HAH 0.95%) are examples. In the U.S. merger arbitrage and managed futures ETFs are several active global macro choices are also available.

Most intriguing are ETFs that reflect what professionals are trying to accomplish using risk and leverage. There is a clear relationship between volatility, as measured by the standard deviation of a market like the S&P 500, and market direction. Stable or falling volatility appears to accompany rising markets while increasing volatility accompanies falling markets. The reason is that volatility is persistent over the short term (autocorrelation = 0.75) and return is not (0.05). This has led to the tracking of VIX, a measure of volatility based upon option premiums. These strategies are not for the retail investor... yet.

Volatility Indices	Symbol	MER
HBP S&P 500 VIX Short-Term Futures™	HUV	0.85%
HBP S&P 500 VIX Short-Term Futures™ Bull Plus	HVU	1.15%

As other professionals study the relationship between groups of securities we expect that their experience will be the same as PŮR's. There are relationships that have always existed but have not yet been exploited. The application of various statistical techniques will lead to new ways to bend and shape risk and ETFs will be the testing ground for these new ideas. The retail investor will benefit in the end because the vehicles will be transparent and available on public exchanges.

The educated consumer is the ETF's best customer today and the product stream of the future will affirm this. In a single digit return environment with pension plans shifting liability to individual and social welfare programmes under challenge, investors must take more responsibility for their financial futures. Advisors need to improve their skills and mutual funds will have to find a new value proposition.

Mark Yamada, President & CEO, PUR Investing Inc.
myamada@purinvesting.com

Investors who experienced the financial crisis and market meltdown in 2009 know that there were few places to hide from the twin forces of volatility and a liquidity vacuum.

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ETF 101: The Basics of ETF Construction

In recent months, exchange-traded funds (ETFs) have faced increasing scrutiny from third-party market commentators, mainly from the U.S.

Oliver McMahon
Director,
Head of iShares Product Management,
BlackRock Asset Management Canada Limited

In recent months, exchange-traded funds (ETFs) have faced increasing scrutiny from third-party market commentators, mainly from the U.S. They claim that some new products being introduced into the marketplace take on dubious structural attributes, which can lead to instability and – worse – total collapse.

We firmly believe that ETFs will never go "bust". The industry has spent over 20 years designing ETFs to ensure that they are robust and will behave as expected, even in times of market stress. An ETF represents ownership of a basket of securities; it trades and settles in the same way as a stock, and its value is tied to the underlying assets it holds. Each ETF is a distinct investment trust, organized under the laws of the province it is governed by. This trust operates under the direction and management of its trustee, a separate legal entity which, in turn, operates under the direction and management of its board of directors or its board of trustees, as applicable. In the case of iShares ETFs, BlackRock Asset Management Canada Limited is the legal trustee. The assets of an ETF are legally held separate from the assets of the trustee, which ensures that the underlying assets that make up the ETF are secure.

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That said, there is no denying that different ETFs can involve different degrees of risk, depending on their structure and investment goals. ETFs can take on a number of unique attributes, depending on how they are constructed. While ETFs can offer a host of benefits such as low fees, transparency, liquidity and easy access to diversification, some investors have inadvertently taken on more risk than intended because they don't have a full appreciation of a particular ETF's structure. In addition, some investors have failed to recognize that not all ETFs are identical, and the features of one ETF may not be shared by another.

Therefore, it is important for investors – and their advisors alike – to understand the fundamentals of ETF construction in order to make a true assessment on whether a product is right for them.

Creation/Redemption Process for Traditional ETFs

First, let's look at the structure of a traditional ETF before we explore some emerging ETF structures. With a traditional mutual fund, an individual investor interacts with the fund when purchasing or redeeming units. The ETF creation process is similar to a mutual fund except that there is an additional participant, the Underwriter or "ETF market maker." To buy an ETF, the following takes place:

- The individual investor, through an advisor/brokerage account, places a buy order. But unlike purchasing a mutual fund, his order is directed to the exchange instead of to the fund.
- An underwriter fills the "buy" order by selling units of the ETF for cash. A market maker can then use that cash to replenish their inventory of ETFs through the creation process.

Now, let's look at the creation process. ETF managers, such as BlackRock Asset Management Canada Limited, produce on a daily basis Portfolio Composition Files (PCFs) for each of their funds. These files list the exact stocks held by an ETF in their representative percentages. As the ETF market makers sell ETFs to buyers in exchange for cash, they use the PCFs to determine which stocks they must buy to implement a hedge. Eventually, the market maker will need to "create" new units of the fund. To do this, they must deliver the shares listed in the PCF to the fund. This occurs through an "in-kind" transfer, whereby the fund gets additional stocks, and in turn issues more units. This mechanism operates continuously, which normally eliminates meaningful impact to the underlying securities' markets.

The redemption process works the same way, but in reverse.

The Cost Efficiency of ETFs: Beyond the Management Fee

Investor advocates have long touted the economic benefits of ETFs in comparison to actively managed mutual funds. Cost is important because fees are deducted straight out of an investor's return. ETF transactions will result in brokerage commissions, but the savings from lower annual fees can help offset these costs for long-term holders. Another consideration is that the cost of acquiring the underlying securities for the fund is included in the ETF's own bid/ask spread, which benefits both short- and long-term investors.

ETFs enable price specificity and hedging capabilities not available with traditional mutual funds. For example, intraday pricing enables investors to place limit orders on purchases or sales and execute in real time; stop orders can be entered and investors can even sell ETFs short (standard margin rules apply).

The continuous pricing feature of ETFs is significant in that – unlike traditional open-end mutual funds – ETFs offer the same intraday liquidity as other securities that trade on major exchanges. The trading price of an ETF is therefore determined on a continuous basis (in reference to the ETF's holdings). The transparency of these holdings enables premiums and discount to NAV to correct very quickly through arbitrage, where the supply of outstanding shares is increased or decreased based on changes in demand. The benefit to investors is efficient pricing on an intra-day basis. Thus, implementing asset allocation strategies with open-end funds is no longer limited to end-of-day execution.

Costs are a key consideration when selecting an ETF. The expense ratio, which covers the costs of fund management, trustees, licensing and operational costs, is only one element of an ETF's total cost. Investors should also consider the impact of implicit costs such as bid/ask spreads, portfolio rebalancing within an ETF, and the ETF's tracking error relative to the benchmark. Implicit costs are not equal across ETFs and can easily exceed any explicit cost advantage of one ETF over another.

Know Your Index: Market Capitalization, Fundamental and Equal-Weighted

Most ETFs traditionally follow a market capitalization strategy, in that they weight securities in proportion to the market capitalization of their respective index, e.g., S&P 500 Index, the Russell 3000 Index and the MSCI EAFE Index.

In recent years, several alternatives to traditional market-capitalization-weighted indexes have emerged, such as equal-weighted and fundamental indexing. Fundamental indexing is a strategy for investing that weighs securities proportionally to fundamental measures of size such as cash flow, sales, book value and dividends. As the name implies, equal-weighted indexing is comprised of every stock in the index having the same weighting regardless of the company's market capitalization or fundamentals.

There are some factors to consider if an investor decides to pursue a non-market capitalization strategy. Non-market capitalization-weighted indices generate primitive "active" exposure in that they are intended to outperform capitalization-weighted benchmarks i.e., generate alpha. There is no guarantee that the additional risk will be compensated with a higher return. In addition, fundamentally-weighted indices typically have a smaller-cap tilt and a bias toward value stocks. Performance therefore is heavily influenced by differences in the returns of value, growth and sector trends in the market. For example, in periods where value outperforms growth and small outperforms large, fundamentally based indices should outperform. Investors should be aware however, that this performance comes from sector and style biases. In contrast, market capitalization indices express no market view and reflect the aggregate perspective on stock price valuation of all market participants.

Proponents of non-market-cap-weighted indexing contend that cap-weighted indices overweight the overpriced securities and underweight the underpriced securities. It follows then that a portfolio weighted according to true values, if such values could be determined, would outperform a traditional cap-weighted index when the pricing errors finally correct. They further argue that weighting by fundamental measures of size corrects the negative impact of these pricing errors. The challenge is that it is difficult to identify and improve estimates of true value when constructing portfolios because many opportunities are hard to identify, are quickly arbitraged away or are simply not scalable.

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While there is nothing wrong with the investment merits of non-market-capitalization strategies, investors must be aware of the differences. Equally important, investors must remember that past performance is not necessarily indicative of or a guarantee of future results.

Beyond the Traditional ETF: Understanding Alternative ETF Structures

Innovations in product structure have allowed the expansion of the traditional open-end fund design traditionally associated with ETFs. Each structure has unique exposure and risk implications. Investors need to understand these nuances to select products that are appropriate for them. Knowing how an ETF is constructed is crucial to understanding the performance, tax properties, risks and costs of that ETF.

Many ETFs, particularly in Canada, achieve their investment results by investing in other ETFs, such as those domiciled in the U.S. This design can be a highly efficient way to invest in foreign markets (perhaps in combination with a currency hedge), and also a strategy for building ETFs with a diversified asset mix. Note however that when considering a “fund of fund” structure, investors should be sure to consider management fees charged at both the top and bottom fund level before investing.

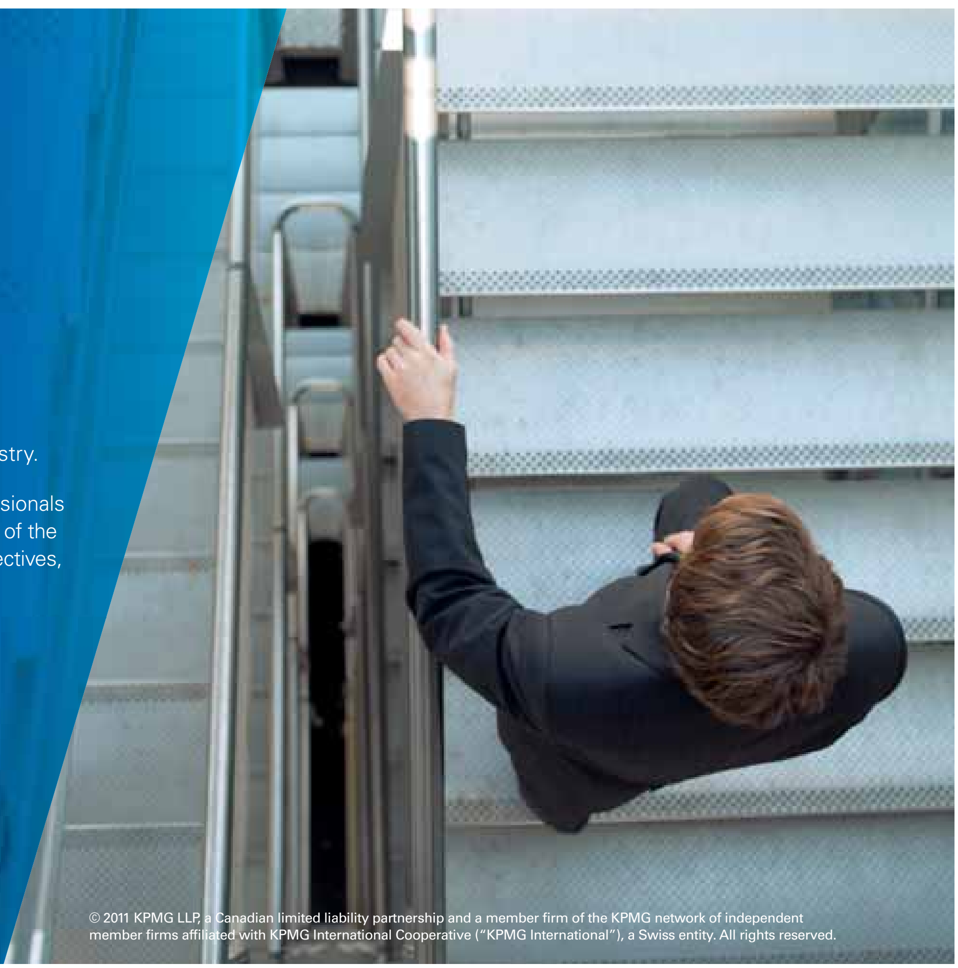
Other approaches to ETF structure include utilizing futures, swaps or other derivative instruments to achieve their exposures. ETF providers in Canada have started to introduce products that, instead of holding bonds or stocks directly, hold forward contracts or swaps that are linked to an index. In this structure, the ETF enters into a contract with a third party, typically a bank, whereby the bank is obligated to pay to the fund the return on a particular index or portfolio. The fund in turn holds collateral (usually cash instruments and sometimes equities) in its portfolio. These strategies therefore introduce, often unknowingly to investors, counterparty risk: the danger that the counterparty will be unable to honour its obligations under the contract. Swaps can also involve liquidity constraints since there are no centralized markets for trading or clearing swaps. Leveraged ETFs, in addition to being exposed to volatility through daily resets of leverage, are an example of products that employ these types of derivative strategies.

Some ETF providers are also introducing products that, while holding bonds or stocks directly, utilize “active” managers, instead of tracking “passive” indices, to achieve returns.

While there are many valid rationales for such strategies, there can also be additional risks and costs. Transparency is another concern, especially with active portfolios, as the portfolio composition may not be immediately available to the investor. In addition, the tax consequences of such products should be carefully researched and understood. While the economic exposure is equal to directly investing in stocks or bonds, the tax consequences can be significantly different.

Again, while there is nothing inherently wrong with any of the ETF structures or philosophies discussed earlier, their existence does suggest the investor must carefully research and understand the intricacies of a product before investing. This may mean getting back to the basics in knowing the fundamentals of ETF construction. The more knowledge the investor holds, the less likely they will be swayed by misconceptions and the more likely they will be able to ensure that the products that they have selected are right for them.

Oliver McMahon, Director, Head of iShares Product Management, BlackRock Asset Management Canada Limited
oliver.mcmahon@blackrock.com



Be Cautious With Commodity ETFs

Before speculating on oil prices with futures-based ETFs, take a moment to look under the hood; you might be surprised at what you're actually buying.

John Gabriel
ETF Strategist - Canada, Morningstar, Inc.

Commodities can play a role in a balanced asset allocation. A track record of providing uncorrelated returns has won the commodity category a place in many portfolios as an attractive diversifier in a mix with stocks, bonds, and cash.

ETFs have made a category that was once the realm of large institutional investors accessible to the masses. But, as with everything, investors should be aware of what they are actually buying when they go shopping for a commodity-focused ETF. A look behind these funds' label will show that they are often not what they seem.

Odds Are It's Not Spot

Spot prices are the stuff of commodity headlines, the numbers called out every day in the financial media, and represent the prices for immediate payment and delivery on everything from natural gas to zinc. Many investors are under the impression that commodity ETFs will provide them exposure to changes in the spot market prices of copper, corn, oil, wheat, etc. In the vast majority of cases, this simply isn't so. Unless you are buying a fund that takes physical possession of the underlying commodity, you are not receiving direct exposure to spot market prices. There are currently ETFs tracking gold, silver, platinum, and palladium that directly hold their reference metals. Given that these metals are fairly simple to standardize and inexpensive to store (high value-to-weight ratio), they lend themselves well to a physical holding structure. Also, you don't have to worry about gold bullion spoiling the way you do soft commodities like wheat or corn.

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A Look Into The Futures

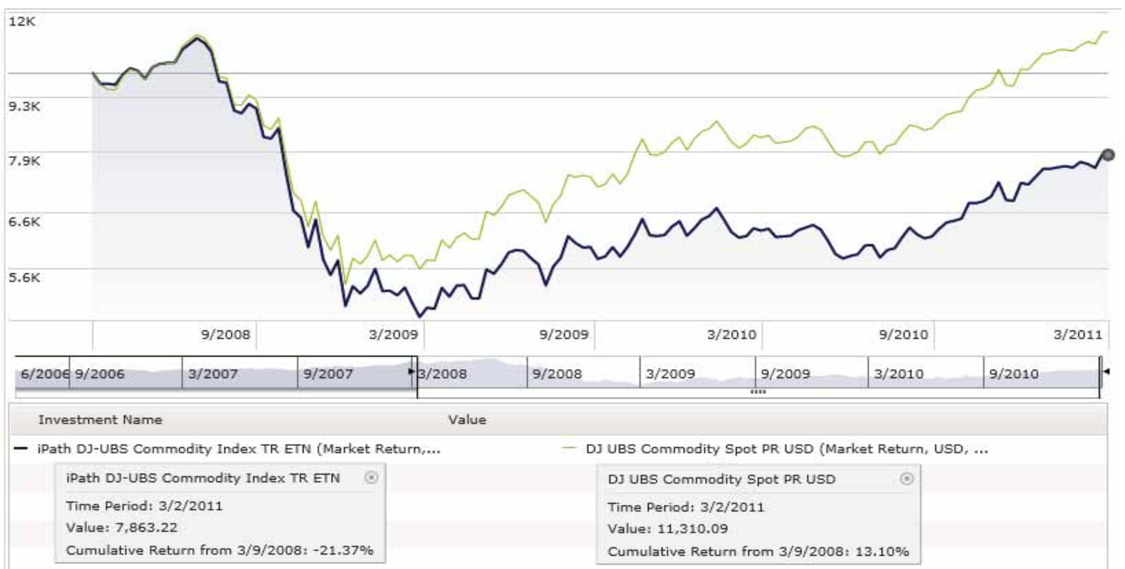
So if the commodity ETF doesn't track a commodity's spot price movements and it isn't taking physical possession of the underlying commodity, what exactly are you getting? Most commodity ETFs provide exposure to movements in the prices of futures contracts traded on a single commodity (oil, natural gas, copper, etc.) or an index comprised of single-commodity futures (DJ-UBS Commodity Index, S&P GSCI Agriculture Index, etc.). Futures contracts represent an agreement to buy or sell a commodity at a pre-determined date and at a pre-determined price. Futures prices will differ from spot prices based on a number of different factors including storage costs (paying for oil tankers, grain silos, etc.) and seasonal demand patterns (natural gas futures might rise above spot prices in anticipation of a cold winter), amongst others. As such, the returns on ETFs investing in commodity futures will typically differ from the spot price returns of the underlying commodity or basket of commodities.

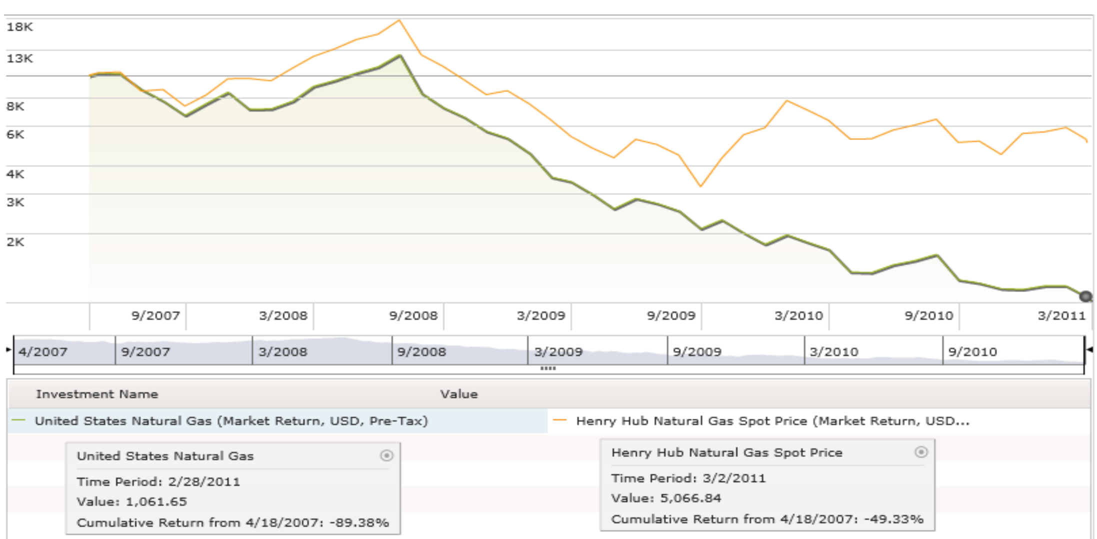
Roll Returns

Further distorting the performance between the prices of commodity futures funds and spot price movements is the fact that commodity funds must periodically roll into new futures contracts as existing contracts expire. For instance, a fund that provides exposure to 1 month forward Brent oil will have to sell out of one month's futures contracts and buy the subsequent month's contracts on a regular basis.

The regular rolling of futures contracts results in what is known as roll returns or roll yield. This is the source of the majority of the difference between spot price returns and the returns experienced by investors in commodity futures. Roll return can be attributed to the price difference between the current period's futures contracts and the price of the subsequent periods' contracts into which the fund or index is to be rolled. Roll returns can be either positive or negative depending on the slope of the futures curve for the commodity or index in question. If the futures curve is upward sloping--that is each subsequent months' futures price is progressively higher (known as contango) – this will result in a negative roll yield.

How does this work? Each period the fund will sell relatively low priced contracts and buy relatively higher priced contracts further out on the futures curve. The process of selling low and buying high results in negative roll yield. This phenomenon has been prevalent of late, as many commodities futures markets have been in contango for the past couple years. The devastating effects can be seen in the following graphs.





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But what if the futures curve is downward sloping, or backwardated? Backwardation results in a positive roll yield. Each period, the fund will sell relatively higher priced contracts and buy relatively low-priced ones. Historically, most commodity markets sat in backwardation. However, increased participation in commodities markets by non-producers in recent year may have altered the dynamics of these markets for good.

What Are The Implications Of Roll Yield?

Roll yield will lead the returns of commodity futures indices and funds to diverge from commodities' spot price performance. As you can see in the graph below, while natural gas prices rallied in the back half of 2009 and into 2010 (represented here by the spot price returns of Henry Hub Natural Gas), futures-based ETF United States Natural Gas UNG posted sharply negative returns. However, this is not attributable to a flaw in the fund's design. They performed exactly as advertised. The wide divergence in returns here is due to the fact that the natural gas futures curve has had a steep upward slope over the last couple of years, resulting in negative roll returns which weighed heavily on the fund's performance.

How Do You Deal With Roll Yield?

Creating a better way to replicate the spot price performance of a broader swath of commodities is the Holy Grail for commodity fund providers. Given the costs of storage, a physical replication fund for oil, natural gas, or agricultural products is an unlikely solution. However, there are a few unique options currently on the menu that seek to tackle some of the challenges associated with investing in commodities through futures markets.

The first fix is to simply invest in futures that are further out (say 12 months) on the curve. Investing in longer-dated futures contracts can do a bit to mute the effects of regular rolling which are typically most pronounced in front month futures. However, this strategy isn't foolproof, and real results are mixed at best, as you can see in the following graph. United States 12 Month Oil USL declined in value, despite the fact that spot prices were slightly positive over the same period.

There are more advanced strategies available that actively seek to minimize roll losses when futures markets are in contango and maximize roll gains when they are in backwardation. For instance, Claymore recently launched its Claymore Broad Commodity ETF CBR, a futures-based commodity ETF that tracks an index which uses a rules-based quantitative strategy to manage the process of rolling futures positions in their component commodities.

The level of diversification provided by the fund, coupled with a proven measure to manage roll returns makes these funds an attractive option for a portion of one's long-term commodity allocation, in our opinion.

Buyer Beware

ETFs have opened commodity markets to a broader swath of investors. While the democratization of this asset class can benefit all market participants, it has been accompanied by a good deal of confusion amongst those new to the sector and to the ETFs that track it. Investors should be wary of commodity-focused ETFs. Those looking for spot price exposure must recognize that spot prices do not represent an investable return. The closest proxy for spot price performance comes through physical holdings – which are presently limited to precious metals funds in the ETF category. Outside of physical holdings, ETF investors are purchasing exposure to the movements in commodity futures prices. Investing in commodities through futures introduces unique considerations and sources of return (both positive and negative) – most notably roll returns. For a long-term position in commodities, we think that some of the best ETF options in the category include funds like Claymore Broad Commodity ETF, which offers exposure to a broad, well-diversified basket of commodities in tandem with a tested strategy for managing roll returns.

John Gabriel, ETF Strategist - Canada, Morningstar, Inc.
john.gabriel@morningstar.com

Outside of physical holdings, ETF investors are purchasing exposure to the movements in commodity futures prices.

2011 CALENDAR OF EVENTS

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Exchange Traded Forum

Tuesday, May 10 & Wednesday, May 11, 2011 – Toronto
Monday, June 20, 2011 – Calgary
Wednesday, June 22, 2011 – Vancouver

ETFs, ETNs, Indexing

In it's second year, the **ETF** conference will address the latest trends and developments in this rapidly changing and growing sector. The agenda features industry experts sharing their experiences and forecasts in a format designed for retail and institutional investment professionals.

EXCHANGE TRADED FORUM 2011

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Niagara Institutional Dialogue

Monday, June 13 to Wednesday, June 15, 2011 – Niagara-on-the-Lake

Niagara Institutional Dialogue is an exchange of ideas, knowledge and practices for Canadian Institutional Investors. A selected group of senior representatives from Canadian pensions, will participate in three days of informative discussions, education and networking.

This confidential closed door event is reserved for select industry participants.

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10th Anniversary World Alternative Investment Summit Canada

Monday, September 19 to Wednesday, September 21, 2011 – Niagara Falls

WAISC is Canada's largest annual gathering of alternative and exempt market investment professionals and service providers. Featuring panel discussions with top-level international speakers, fund managers and leading service providers, WAISC brings together over 400 delegates to explore every side of the alternative and exempt market investment space.

WAISC 2011
World Alternative Investment Summit Canada

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10th Anniversary!

Mutual Fund & Insurance Summit Canada

Monday, October 17 & Tuesday, October 18, 2011 – Toronto

The mutual fund and insurance industries are constantly evolving and creating new ways to stay attractive to serious investors. This Summit is an ideal opportunity to stay on top of trends, topics and products. This two day event will focus on educating developing and seasoned advisors as well as industry participants in what is current and will update on themes from the past. This is the ideal opportunity to meet, learn and network with your peers as well as be educated in new trends.

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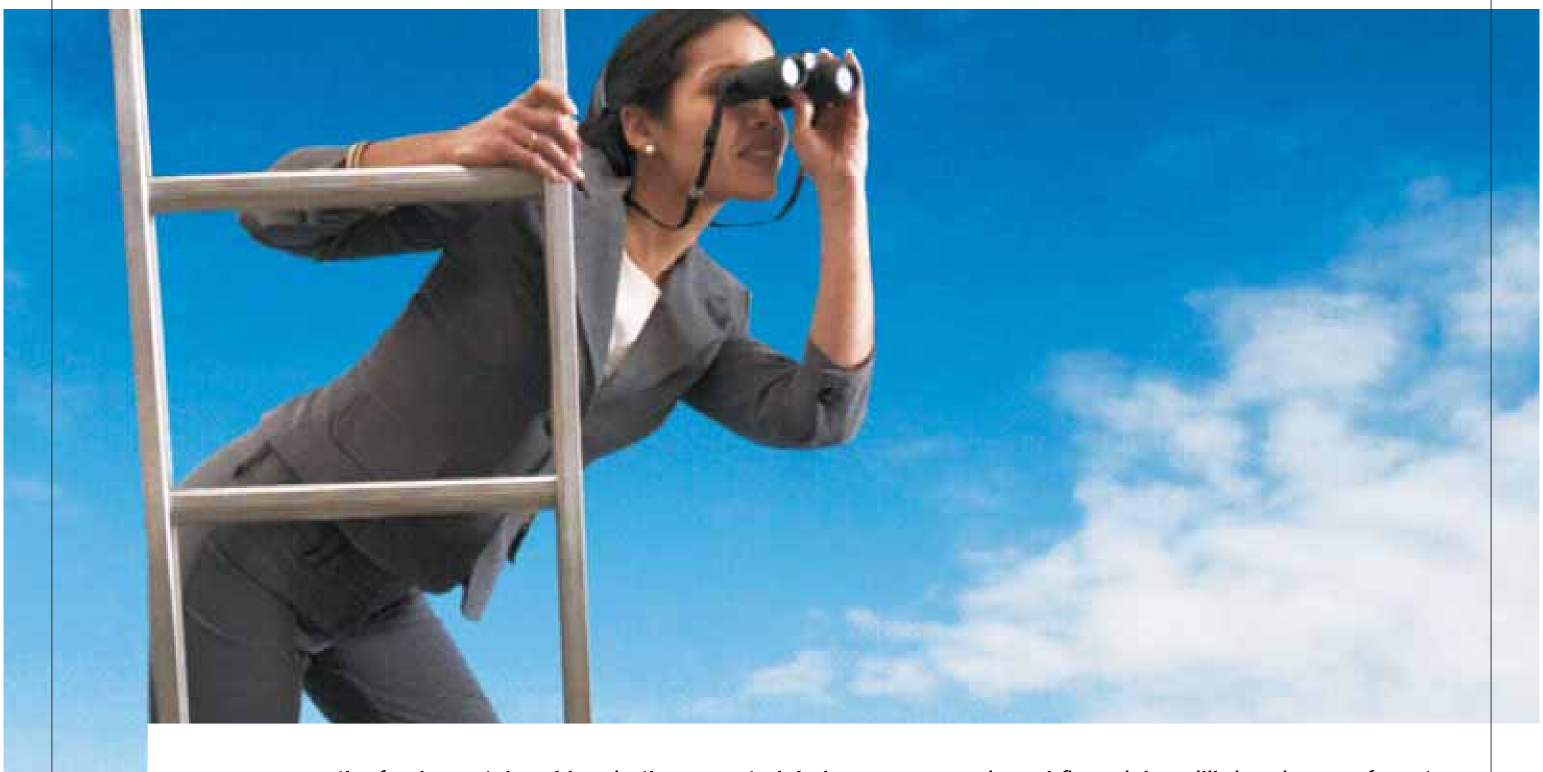
Are "Safe Assets" In Short Supply?



Tyler Mordy
Director of Research, Horizons HAHN Investment Stewards & Company Inc.

… the fundamental problem in the current global macroeconomic and financial equilibrium is one of asset shortages. In particular, there is a shortage of safe "AAA" assets. The world seems to need more US Treasury-like instruments than are available.

False emperors (AAA assets) are created, and it is only later on that we discover these emperors have no clothes. In fact, the recent difficulties in the Eurozone can be seen in this light, with Greece and others dropping from the potential safe-asset producers list."

>> **Ricardo Caballero**, Professor of Economics, MIT

Is the world suffering from a chronic shortage of "safe assets"? That's the assertion of MIT Economics Professor Ricardo Caballero. In a series of research papers,[1] Caballero has argued that the supply of safe assets is not keeping pace with global demand.

How so? At the heart of Caballero's theory lies the enormous wealth creation of emerging markets and oil-exporting economies. While these countries have seen rapid increases in wealth and disposable incomes, their ability to generate quality assets to store that wealth has been severely limited. On the opposite end, developed Anglo-Saxon economies – with their mature capital markets, strong rule of law, and low risk of expropriation – have been successful in producing safe financial assets… even as overall growth and savings rates have lagged.

HORIZONS
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Before we investigate the theory, it helps to define some terms. What exactly is a "safe" asset? True, safety can be somewhat subjective… and, it is a status often driven by collective investor opinion. *(It brings to mind Judge Potter Stewart's famous definition of hard-core pornography – "I know it when I see it.")* Yet, while it can be a vague definition and applied capriciously, the focus should be on assets with low default risk and high liquidity.

What about the safety of ETFs? Here, allow us to dismantle a persistent misconception surrounding ETFs. Many investors wrongly assume that ETFs introduce additional risk. It's a strange assumption. ETFs are an *investment vehicle*, not a single type of investment. As we have often said, they simply "wrap" a number of different types of investments in an efficient structure *(more tax efficient, lower cost, etc.)*. What's more, ETFs are normally structured as trusts with a third-party custodian holding the underlying assets on behalf of the unit holders. Viewed in this light, the ETF vehicle itself is solid. The relevant question is what assets are being held and tracked by the individual ETF?

Safety First?

Let's return to Caballero's thesis. Under his framework, the implications are many. For one, asset bubbles will be a recurring feature in global financial markets.Excess world savings and the honest hunt for safe assets will periodically erupt into speculative episodes. Past consequences range from increasing the "leverage equilibrium" of the average Anglo-Saxon household *(due to depressed interest rates)* to spawning the sub-prime securitization boom that occurred in the first part of the last decade *(read: packaging and redistributing questionable mortgage debt as an attempt to meet safe asset demand).*

Whether you agree with Caballero or not, this supply/demand imbalance has been aggravated by the recent financial crisis. Both uncertainty and demand for safe assets has remained elevated since 2008. In fact, private investors spent most of 2009 and 2010 sitting on the sidelines *(in cash or fixed income)*. US-listed equity ETFs equities showed net outflows of 26.1 and 15.0 billion for 2009 and 2010, respectively.[2] Others chose gold bullion as a safety alternative, with assets into the SPDR Gold Trust (NYSE:GLD) reaching over USD 56 billion recently.

At this point, the astute reader may inquire about expansionary fiscal policies in the West. Has counter-cyclical fiscal policy not dramatically expanded the supply of "safe" government debt, alleviating soaring demand? Yes, absolutely it has. The supply of US Treasury debt rose a whopping 25% in 2009 alone and the Congressional Budget Office (CBO) just reported a budget deficit of nearly USD 1.7 trillion.

However, the demand side has remained robust, evidenced by falling yields. Data from the US Treasury department shows that domestic investors are increasing their holdings even faster than overseas holders *(the domestic share of the USD 9 trillion in tradable US debt now stands at over 50%)*.

Are investors becoming unnecessarily risk averse in the current climate? In many cases, we think so. Yet, with global interest rates at generational lows and an "unusually uncertain" outlook *(in the words of Chairman Bernanke)*, where should investors be positioned?

This is the dilemma at hand. Our important conclusions we offer in preview: (1) premiums for safe assets are likely to stay high and (2) over time, as capital markets develop and mature in the emerging world, the safety rating is likely to migrate to countries in this sphere… or, at the very least, a significant risk "re-rating" is highly probable in the coming years.

Structural Headwinds Remain

Adopting Caballero's central perspective of a global safe asset shortage, it follows that yields on government debt in many advanced economies will stay low for an extended period. We agree with this conclusion *(even though we think Caballero's safe asset shortage is only one contributing factor).* In fact, we have held this "non-consensus" view for some time.

The heavily dominant consensus among global investors continues to view Western government bonds as a "sell". Yet, most Western government bond prices ended 2010 higher than at the start of the year. The US 10-year now yields 3.38% versus 3.76% at the start of 2010. And, the 2-year note yield hit record lows in 2010, falling under 50 basis points at one point *(never in the Republic's 234-year history has the US government had the privilege of borrowing for 2 years at below half a percentage point).*

What gives? To be sure, the long-term structural outlook in many Western countries is grim, calling for slower growth. The profile of the current recovery is instructive. To date, it has been anything but typical. Employment, income, and capital spending levels are all far below typical post-war recovery norms. For the recovery to develop into a sustainable trend, corporate profits must be reinvested into more efficient technology, new factories and other capital spending outlays. That is what invariably drives economic recoveries and pushes bond yields higher.

Yet, to date, reinvestment of profits is only happening at the margins. Why? For structural reasons, rather than cyclical ones. Spare capacity is high while net consumption is in retreat. The private sector in the West faces an aging demographic, de-leveraging and damaged balance sheets – meaning that overall growth will remain softer than in the past. Corporations, hoarding cash and delaying capital investment, are simply adjusting to a period where the trend in nominal GDP growth will be lower.

These structural headwinds do not mean that temporary reprieves will not regularly surface, intermittently lifting asset prices. The policy-driven stock market rally from March 2009 is a case in point. Indeed, heightened volatility will remain the norm. Yet, the above concerns are completely valid and confirm a long-running premium on safe assets.

Safe Assets: A Moving Target?

How can investors overcome these macro headwinds? As shown, many investors are responding by clinging to traditional safe-havens – mainly cash and government debt in the developed world. We believe this is a misguided response… certainly not foreshadowing decent portfolio returns. Make no mistake, we are not advocating a wholesale portfolio shift into risky assets. We, too, judge that overall risks are higher than normal today. But a better approach is to run diversified, risk-sensitive balanced portfolios, tilting toward assets that have favourable risk/reward dynamics.

Of course, in today's challenging environment, every investor would like all their holdings to be "safe". Regrettably, risk is present in every investment… even ones currently stamped with the coveted AAA rating. The important questions in portfolio management are always twofold: first, is the asset attractively priced for the embedded risk and second, is it suitable within the context of a particular client portfolio?

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Recall our second key conclusion – that is, the quality and perception of asset safety in the developing world will improve dramatically. This does not mean it will happen overnight. The transition from "risky" to "safe" – or, perhaps, to "less risky" – will be a long one. For many investors, this shift will seem paradoxical. After all, emerging markets have always been synonymous with risk. Over the last 30 years, financial crises have always had their epicenter in this group of countries. The Tequila crisis in Mexico, the Russian default, the Asian crisis and the eventual devaluation and default in Argentina in 2001/2002 all had their origins in these markets.

But the current economic issues are centered at the core of the developed nations – the United States and Europe. Yes, there are significant hurdles in the developing world. And, the economic profiles and outlooks are very different from country to country. But many of these countries do not have the same structural imbalances or debt problems that plague developed economies. Past crises were triggered by the usual suspects – debt defaults, currency crises, or hyperinflation. In recent years, those risks have diminished substantially.

Balancing Safety and Risk

Given the above, a useful framework for portfolio management is to ask the following question: which group of assets are likely candidates for a risk "re-rating"? There are a number of possibilities, each driven over the long-term by fundamental factors.

Western multinationals are leading contenders here. These stocks have been neglected for years, yet are world-beating enterprises that operate under strong corporate governance standards and stand the best chance of weathering the current economic climate. Debt burdens are clearly less than governments and households, and revenue streams are not dependent solely on domestic sources, deriving a large portion from faster-growing international regions. The mountain of cash on US corporate balance sheets we keep hearing about? That would be concentrated on the balance sheets of the largest mega-cap companies. And, generally speaking, valuations are much more attractive than their smaller cap brethren *(ETFs supply exposure here – e.g. DLN on NYSE).*

As we have discussed, other likely entrants into the safe *(or "safer")* list include select investments in the emerging world. And, they may start supplying AAA assets sooner than most think. Of course, an increase in supply of assets isn't always directly positive. Yet, if the supply can increase whilst at the same time quality ratings are improving, then we have a positive trend. The marketplace for emerging market government debt denominated in local currency has been rapidly growing, now over USD 1,000 billion. In 2003, that figure was less than USD 200 billion.[3] At the same time, returns have been less volatile while credit upgrades have been commonplace. Previously inaccessible through ETFs, two such trackers were launched in August 2010 *(NYSE:ELD, EMLU).*

Emerging equity markets have also shown less volatility in recent years. Traditionally, they have always been "high-beta" plays on Western stock markets and the global business cycle. Yet, betas have been trending down for the last few years. In the recent global equity market selloff, betas actually declined.

A corollary to the above asks the opposite question: which assets risk losing their safe-haven status? Greek sovereign debt is a recent example. Of course, many advanced countries will continue to retain their safe ratings. Others will not.

Conclusions

Given ongoing high growth rates in the emerging world, Professor Caballero predicts that the safe asset shortage will persist. His policy prescriptions focus on expanding the supply of AAA assets. How to achieve this? In the long run he concedes that supply must originate in emerging markets. More immediately, he recommends two strategies. First, expand the supply of government debt. Check. Second, allow the private sector in Anglo-Saxon countries to produce safe assets, but provide an implicit government guarantee against extreme systemic events *(i.e. raising the safety perception of these assets).*

Of course, the first recommendation is not a sustainable one. Government debt cannot expand indefinitely… or, if it does, the country risks losing its safety status. We expect that Greece, Portugal and Ireland will not be isolated cases. As for the second recommendation, we are not holding our breath. A government-led program of that size would take years to implement *(and, we are doubtful it could be organized effectively).*

All of which unfortunately leads us back to the same safe asset shortage conundrum. That ensures "macro" volatility will remain higher than normal in the coming years. Nevertheless, the long run outlook remains encouraging for many emerging economies. The comparative headwinds in these major countries will be less severe given lower debt levels, intact banking systems and broadly favourable demographics. As for the assets of these countries, the "safety" label may be applied sooner than most think.

Tyler Mordy, Director of Research, Horizons HAHN Investment Stewards & Company Inc. ***tmordy@hahninvest.com***

Endnotes:

[1] Caballero, Ricardo. "On the Macroeconomics of Asset Shortages." November 2006. http://www.nber.org/papers/w12753

Cabellero, Ricardo and Arvind Krishnamurthy. "Global Imbalances and Financial Fragility." December 2008. http://www.nber.org/papers/w14688

[2] Figures from the National Stock Exchange through to end February 2011.

[3] As measured by the JPMorgan GBI-EM Broad index.

Given ongoing high growth rates in the emerging world, Professor Caballero predicts that the safe asset shortage will persist.

Commodities In Portfolio Construction

Over the last decade, commodity and commodity-related investments have gained significant popularity with both institutional and retail investors. Given their sizable returns over the last ten years, historical low correlation to traditional asset classes and emerging markets soaking up much of the supply, it should not come as much of a surprise.

Alfred Lee
Investment Strategist, BMO ETFs & Global Structured Investments

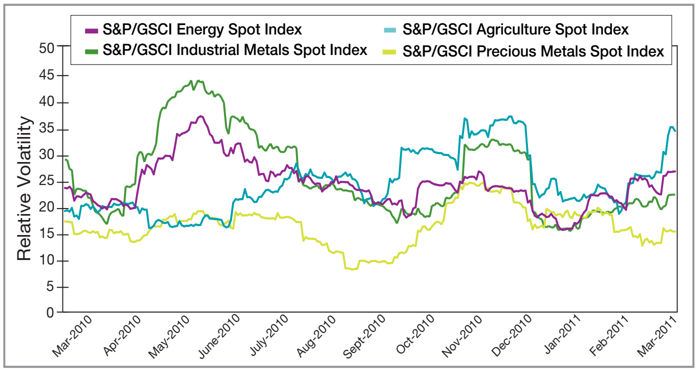
Coming out of the credit crisis, major central banks around the globe, most notably the U.S. Federal Reserve (Fed), were focused on reflating the global economy.

The co-ordinated easy monetary policies, government stimulus measures along with quantitative easing were largely a positive for broad commodities which tend to be used as a hedge against declining currency values and particularly a falling U.S. dollar. Essentially, investors benefited from merely having exposure to a broad basket of commodity and commodity related investments. With global stimulus and the second instalment of quantitative easing1 (QE2) moving further into the rear-view, the reflation trade should be less of a driver in global commodity prices going forward, especially considering the Fed is anticipated by some to remove QE2 stimulus this summer. Independent supply and demand fundamentals as a result should play a more important role in driving commodity prices going forward. In addition, with political turmoil in the Middle East and now the unfortunate tsunami in Japan, these issues will have different macro factors on the varying commodity sub-groups.

Commodity Differentiation

With that in mind, investors may want to consider commodity differentiation at this point in their portfolio construction process. As global economic fundamentals slowly improve, correlation between assets and within assets such as commodities should naturally decrease (as detailed in the correlation matrices shown) in an economic thawing process. Moreover, as previously mentioned, the negative headlines will have varying impacts and ramifications on each of the commodity groups. Investors should therefore focus on commodities that have the best risk-adjusted returns and those which will further optimize their overall portfolio.

Commodity Sub-Groups React Differently To Macro-Risk



As many investors are aware, the proliferation of exchange traded funds (ETFs) and exchange traded products (ETPs)2 have allowed investors to efficiently implement commodity exposure to their portfolios in a number of different ways. Through ETFs and ETPs, investors can access commodity futures, commodity related companies and in some cases, spot prices. Investors should however first be cognisant that different commodity sub-groups react differently to macro-economic events and each also has its own fundamental and technical trading patterns. Secondly, how each ETF or ETP structure reacts to these same macro-events can also be different based on how it is accessing the specific underlying commodity (ie through spot, futures or equities).

As many investors are aware, the proliferation of exchange traded funds (ETFs) and exchange traded products (ETPs)2 have allowed investors to efficiently implement commodity exposure to their portfolios in a number of different ways.

Some Commodities Have Become Less Correlated

Year to Date
Correlation Matrix: December 31, 2010 to March 21, 2011

	S&P GSCI	Energy	Industrial Metals	Agriculture	Precious Metals
S&P GSCI	100.0%	95.0%	35.3%	55.3%	55.2%
Energy	95.0%	100.0%	16.5%	27.9%	56.3%
Industrial Metals	35.3%	16.5%	100.0%	44.9%	10.1%
Agriculture	55.3%	27.9%	44.9%	100.0%	14.3%
Precious Metals	55.2%	56.3%	10.1%	14.3%	100.0%

Period of Reflation
Correlation Matrix: March 9, 2009 to January 1, 2011

	S&P GSCI	Energy	Industrial Metals	Agriculture	Precious Metals
S&P GSCI	100.0%	98.4%	68.3%	61.3%	43.7%
Energy	98.4%	100.0%	59.9%	48.6%	38.1%
Industrial Metals	68.3%	59.9%	100.0%	46.1%	40.7%
Agriculture	61.3%	48.6%	46.1%	100.0%	33.1%
Precious Metals	43.7%	38.1%	40.7%	33.1%	100.0%

Pre-Credit Crisis
Correlation Matrix: December 31, 1999 to June 30, 2008

	S&P GSCI	Energy	Industrial Metals	Agriculture	Precious Metals
S&P GSCI	100.0%	97.9%	39.7%	47.1%	52.2%
Energy	97.9%	100.0%	26.2%	33.5%	44.1%
Industrial Metals	39.7%	26.2%	100.0%	23.1%	48.7%
Agriculture	47.1%	33.5%	23.1%	100.0%	31.5%
Precious Metals	52.2%	44.1%	48.7%	31.5%	100.0%

Source: Bloomberg, BMO Asset Management Inc.
*Commodity classes represented by S&P/GSCI Spot Commodity Indices and priced in USD. Correlation figures calculated using daily data.

For further information on the advantages and disadvantages of each commodity ETF/ETP structure, please see the ***"Gaining Commodity Exposure Through ETFs"*** on our website. **http://www.etfs.bmo.com/**
In the following pages, we will outline our fundamental and technical outlook on four major commodity subgroups: agriculture, base metals, energy and precious metals.

Agriculture

As we mentioned at the beginning of the year in our ***BMO ETF 2011 Outlook Report***, food price inflation will be a topic du jour this year, with global population anticipated to hit seven billion and the rising wealth in the emerging nations continuing to place upward pressure on soft commodity prices. Furthermore, extreme weather patterns over the last year in Australia and Latin America will lead to tighter supplies. Already this year, we have seen the future contracts of a number of soft commodities such as wheat hit its limit up3 in trading. Now with a number of agriculture commodity contracts such as wheat, corn and soybeans currently trading in backwardation4 or in mild contango5, we prefer attaining soft-commodity exposure through futures based ETFs/ETPs. Some agriculture related companies may experience expansion at the middle portion of their income statements should they not be able to pass full grain cost appreciation to consumers. As a result, futures may provide a more pure exposure to higher agriculture prices considering the current characteristics of the commodity curve. We would caution however, that with the strong run up in many of the agriculture contracts, we would look at technical indicators such as RSI6 and MACD7 for entry points.

Potential Investment Opportunities:

- ***BMO Agriculture Commodity Index ETF (ZCA) – on pullbacks.***

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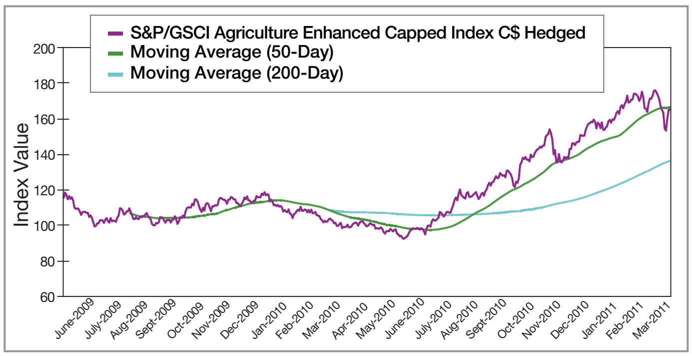
Commodity Sub-Groups React Differently To Macro-Risk

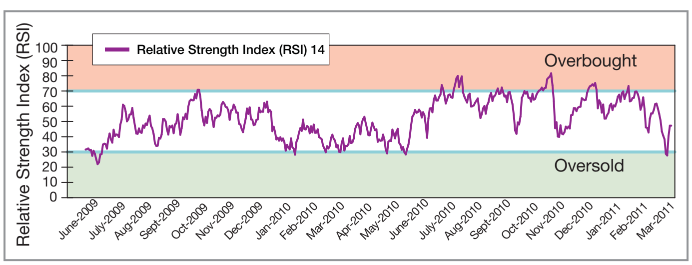
Agriculture Futures Curve Characteristics	
Commodity	**Current Commodity Curve Characteristics**
Wheat	Contango
Sugar	Backwardation
Corn	Near-month contango, further-month backwardation
Soybean	Backwardation
Cotton	Backwardation
Coffee	Near-month contango, further-month backwardation
Kansas Wheat	Near-month contango, further-month backwardation
Cocoa	Backwardation

Source: Bloomberg, BMO Asset Management Inc.
(Commodities based on futures contracts trading on the Chicago Board of Trade, ICE Futures Exchange and Kansas City Board of Trade)

Commodity Sub-Groups React Differently To Macro-Risk



Source: Bloomberg, BMO Asset Management Inc.



Source: Bloomberg, BMO Asset Management Inc.

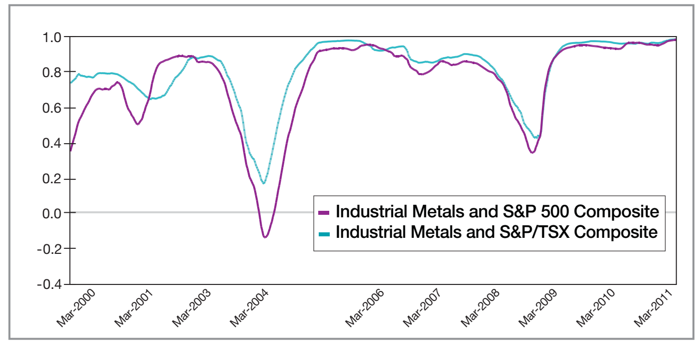
Base Metals

Base metals as a group saw very sizable returns in 2009 with the S&P/GSCI Industrial Metals Spot Index gaining 91.2%. As copper, zinc and nickel are largely tied to industrial production, prices in these metals are rather sensitive to economic expansion. In addition base metal prices are highly correlated to stock market sentiment, given equity values on a whole are also a leading macro-economic indicator. In 2010, volatility in equity market sentiment with investors switching frequently between the "risk-on" and "risk-off" trade, led base metals as a group to lag other commodity groups. We are the least favourable on base metals when looking for assets to best optimize a portfolio's risk/return characteristics because of the high correlation between copper, zinc and other industrial metals to equity prices.

Moreover, as we see equity market volatility shocks to be a common theme this year, base metal future trades should be utilized more for higher-beta momentum trades based on timing than portfolio construction building blocks. For investors looking for base metal exposure, we do however currently favour futures based ETPs over equity-based ETFs as base-metal related companies have run significantly against the S&P/GSCI Industrial Metals Spot Index. The futures curve characteristics for base metals are mixed with a number of contracts recently moving to a steeper backwardation. Nevertheless, products incorporating a "smart-roll" feature that look to reduce roll effects should be considered by those desiring exposure in this area.

Potential Investment Opportunities:
• BMO Base-Metals Commodity Index ETF (ZCA)
– for momentum based trades.

Base Metals Highly Correlated to Equities



Source: Bloomberg, BMO Asset Management Inc.

Base Metals Futures Curve Characteristics

Base Metals Futures Curve Characteristics	
Commodity	**Current Commodity Curve Characteristics**
Copper	Near-month contango, further-month backwardation
Zinc	Backwardation
Aluminum	Contango
Nickel	Near-month contango, further-month backwardation
Lead	Backwardation

Source: Bloomberg, BMO Asset Management Inc.
(All commodities based on futures trading of London Metals Exchange)

Energy

Energy prices remain one of the wildcards in the revival of the global economy. Should Brent crude prices and, to a lesser extent, West Texas Intermediate (WTI) defy gravity for a sustained period of time, it could potentially put the brakes on the global recovery as higher oil prices would increase everything from costs of production inputs to transportation. However, much of the recent rise in crude prices is also a result of the markets pricing in a risk premium and an emotional element, seen through a widening gap between implied and realized volatility on crude.

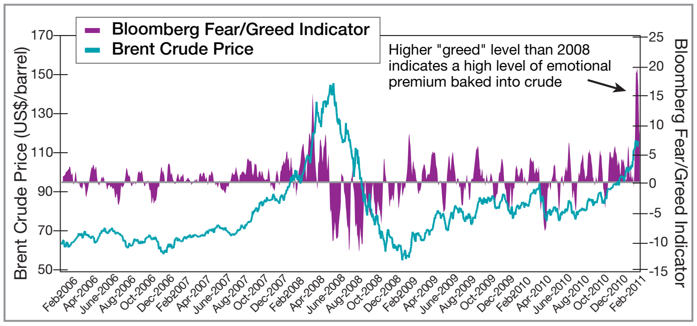
Investors with an extremely short-term horizon may want to consider futures-based energy ETPs. Though we wouldn't be surprised to see the price of Brent crude and WTI rise further, it comes at a higher risk/reward trade-off given the sizable amount of emotion that is currently priced into oil. Last month, when rumours that Libyan leader Muammar Gaddafi was shot broke out, the emotional premium in oil prices quickly dissipated before rapidly recovering after the news was declared false. This demonstrated the excessive level of political premium currently built into crude prices. An investment in crude through futures is therefore an indirect bet that turmoil in the Middle East will continue. Additionally as we had forecasted back in January, higher crude prices would come at higher volatility levels this year.

As such, we believe oil related companies have a better risk/reward trade-off at this point, even if they have lagged crude prices as they show a more stable trend and have exhibited lower volatility levels.

Potential Investment Opportunities:

- *BMO Energy Commodity Index ETF (ZCE) – Shorter-term investors*
- *BMO Junior Oil Index ETF (ZJO) – Longer-term investors*

Significant Emotional Premium Baked into Oil Prices Still



Source: Bloomberg, S&P/TSX, DEX, BMO Asset Management Inc.

Precious Metals

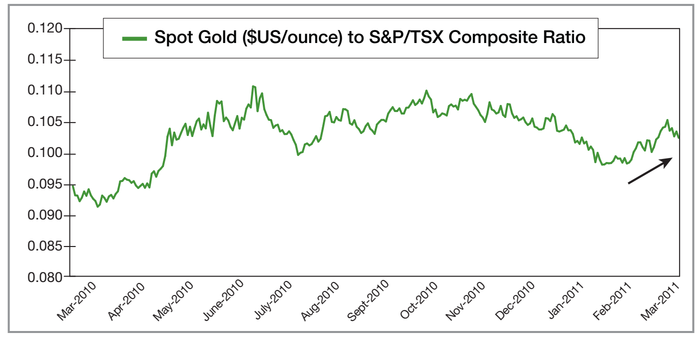
Of the four commodity groups mentioned, precious metals have shown to be the least correlated to broad based equities. The non-correlation to both the S&P 500 Composite Index and the S&P/TSX Composite Index is largely the affect of the market's utilization of precious metals, such as gold, as a multi-purpose hedge. Last year, the sovereign debt crisis and concerns of a global currency war led to the use of precious metals as a hedge against fiat currencies. This year, with food and commodity prices rising, money is slowly transitioning out of the former trade as an alternative currency and into a hedge against inflation concerns.

On a technical level, gold prices have recently shown strength particularly against the equity market and base metals. Within the precious metals sector, small-cap gold companies, which we were extremely bullish on throughout 2010, have recently been gaining relative strength against large-cap gold companies. Investors looking for portfolio diversification may want to consider bullion or ETPs that track gold through bullion or futures, whereas investors looking for ways to generate portfolio alpha should consider junior gold companies.

Potential Investment Opportunities:

- *BMO Precious Metals Commodity Index ETF (ZCP) – Investors looking for portfolio diversification*
- *BMO Junior Gold Index ETF (ZJO) – Investors looking to generate portfolio alpha*

Gold Prices Gaining Against the Equity Market Again



Source: Bloomberg, BMO Asset Management Inc.

In conclusion, we believe commodity exposure will remain an instrumental building block for both institutional and retail portfolios. However, with correlations between commodity sub-groups on the decline, investors should first consider the sub-group of commodities that will best optimize their investment strategy and then determine the investment structure that is best suited to execute their objectives. With the possibility of the removal of QE2 stimulus by the Fed quickly approaching, investors will also need to consider individual supply and demand fundamentals of each commodity since the reflation trade will be less prevalent in keeping all commodities afloat.

Footnotes

1 Quantitative easing: An unconventional monetary policy used by some central banks when traditional measures have not produced the desired effect. Money supply is typically increased in an effort to promote increased lending and liquidity.

2 Exchange-traded products (ETPs): A broader categorization of exchange-traded funds that also include products that hold commodities, futures and other asset types.

3 Limit up: The maximum amount by which the price of a commodity futures contract may advance in one trading day. Some markets close trading of these contracts when the limit up is reached; whereas others allow trading to resume if the price moves away from the day's limit. If there is a major event affecting the market's sentiment toward a particular commodity, it may take several trading days before the contract price fully reflects this change. On each trading day, the trading limit will be reached before the market's equilibrium contract price is met.

4 Backwardation: When the futures price is below the expected future spot price. Consequently, the price will rise to the spot price before the delivery date.

5 Contango: When the futures price is above the expected future spot price. Consequently, the price will decline to the spot price before the delivery date.

6 RSI: Relative Strength Index is a technical momentum indicator that compares the magnitude of recent gains to recent losses in an attempt to determine overbought and oversold conditions of an asset. A reading of 30 or less is generally considered oversold, whereas a reading of 70 or more will be considered overbought.

7 MACD: Moving Average Convergence Divergence: A trend-following momentum indicator that shows the relationship between two moving averages of prices. The MACD is calculated by subtracting the 26-day exponential moving average (EMA) from the 12-day EMA. A nine-day EMA of the MACD, called the "signal line", is then plotted on top of the MACD, functioning as a trigger for buy and sell signals

Alfred Lee, Investment Strategist, BMO ETFs & Global Structured Investments ***alfred.lee@bmo.com***

On a technical level, gold prices have recently shown strength particularly against the equity market and base metals.

ETF FUND PERFORMANCE (as of February 28, 2011)

ETF Name	Ticket	Fund Family	Index	1 Year Return
BMO 2013 Corporate Bond Target Maturity ETF	ZXA	BMO Funds	Not Applicable	
BMO 2015 Corporate Bond Target Maturity ETF	ZXB	BMO Funds	Not Applicable	
BMO 2020 Corporate Bond Target Maturity ETF	ZXC	BMO Funds	Not Applicable	
BMO 2025 Corporate Bond Target Maturity ETF	ZXD	BMO Funds	Not Applicable	
BMO Aggregate Bond Index ETF	ZAG	BMO Funds	DEX UniverseXM Bond Index	-0.4
BMO Agriculture Commodities Index ETF	ZCA	BMO Funds	S&P GSCI Agriculture Enhanced Capped Component Index CAD Hedged	
BMO Base Metals Commodities Index ETF	ZCB	BMO Funds	S&P GSCI Industrial Base Metals Enhanced Capped Commodity Index CAD Hedged	
BMO China Equity Hedged to CAD ETF	ZCH	BMO Funds	BNY Mellon China Select ADR Index CAD	3.1
BMO Covered Call Canadian Banks ETF	ZWB	BMO Funds	Not Applicable	
BMO Dow Jones Canada Titans 60 Index ETF	ZCN	BMO Funds	Dow Jones Canada Titans 60 Index	5.9
BMO Dow Jones Industrial Average Hedged to CAD Index ETF	ZDJ	BMO Funds	Dow Jones Industrial Average (CAD hedged)	6
BMO Emerging Markets Bond Hedged to CAD Index ETF	ZEF	BMO Funds	Barclays Capital Emerging Markets Tradable USD Sovereign Bond Index CAD Hedged	
BMO Emerging Markets Equity Index ETF	ZEM	BMO Funds	Dow Jones Emerging Markets Total Stock Market Specialty Index	-6.3
BMO Energy Commodities Index ETF	ZCE	BMO Funds	S&P GSCI Energy Enhanced Capped Commodity Index CAD Hedged	
BMO Equal Weight REITs Index ETF	ZRE	BMO Funds	Dow Jones Canada Select Equal Weight REIT Index	
BMO Equal Weight U.S. Banks Hedged to CAD Index ETF	ZUB	BMO Funds	Dow Jones U.S. Large-Cap Banks Equal Weight Total Stock Market Index Canadian Dollar Hedged	
BMO Equal Weight U.S. Health Care Hedged to CAD Index ETF	ZUH	BMO Funds	Dow Jones U.S. Large-Cap Health Care Equal Weight Total Stock Market Index Canadian Dollar Hedged	
BMO Equal Weight Utilities Index ETF	ZUT	BMO Funds	Dow Jones Canada Select Equal Weight Utilities Index	1.2
BMO Global Infrastructure Index ETF	ZGI	BMO Funds	Dow Jones Brookfield Global Infrastructure Index	2.1
BMO High Yield US Corporate Bond Hedged to CAD ETF	ZHY	BMO Funds	Not Applicable	3.2
BMO India Equity Hedged to CAD ETF	ZID	BMO Funds	BNY Mellon India Select DR Index CAD	-14.7
BMO International Equity Hedged to CAD Index ETF	ZDM	BMO Funds	Dow Jones Developed Markets ex-North America Index (CAD Hedged)	4.2
BMO Junior Gas Index ETF	ZJN	BMO Funds	Dow Jones North America Select Junior Gas Index	
BMO Junior Gold Index ETF	ZJG	BMO Funds	Not Applicable	-3.6
BMO Junior Oil Index ETF	ZJO	BMO Funds	Dow Jones North America Select Junior Oil Index	
BMO Long Corporate Bond Index ETF	ZLC	BMO Funds	DEX Long Term Corporate Bond Index	0
BMO Long Federal Bond Index ETF	ZFL	BMO Funds	DEX Long Term Federal Bond Index	
BMO Mid Corporate Bond Index ETF	ZCM	BMO Funds	DEX Mid Term Corporate Bond Index	0.8
BMO Mid Federal Bond ETF	ZFM	BMO Funds	Citigroup Canadian Government Bond Index	-0.7
BMO Monthly Income ETF	ZMI	BMO Funds	Not Applicable	
BMO Nasdaq 100 Equity Hedged to CAD Index ETF	ZQQ	BMO Funds	Not Applicable	6.1
BMO Precious Metals Commodities Index ETF	ZCP	BMO Funds	S&P GSCI Precious Metals Commodity Index CAD Hedged	
BMO Real Return Bond Index ETF	ZRR	BMO Funds	DEX RRB Non Agency Bond Index	
BMO S&P/TSX Equal Weight Global Base Metals Hedged to CAD Index ETF	ZMT	BMO Funds	S&P/TSX Equal Weight Global Base Metals Hedged to CAD Index	3.1
BMO S&P/TSX Equal Weight Oil & Gas Index ETF	ZEO	BMO Funds	S&P/TSX Equal Weight Oil & Gas Index	12.1
BMO S&P/TSX Equal Weighted Banks Index ETF	ZEB	BMO Funds	S&P/TSX Equal Weight Diversified Banks Index	7.9
BMO Short Corporate Bond Index ETF	ZCS	BMO Funds	DEX Short Term Corporate Bond Index	0.3
BMO Short Federal Bond Index ETF	ZFS	BMO Funds	DEX Short Term Federal Bond Index	0
BMO Short Provincial Bond Index ETF	ZPS	BMO Funds	DEX Short Term Provincial Bond Index	0
BMO US Equity Index ETF	ZUE	BMO Funds	Dow Jones U.S. Large-Cap Index (CAD hedged)	5.6
Claymore 1-5 Yr Laddered Corporate Bond ETF	CBO	Claymore	DEX 1-5 Yr Corporate Bond Index	0.3
Claymore 1-5 Yr Laddered Corporate Bond ETF (Advisor Class)	CBO.A	Claymore	DEX 1-5 Yr Corporate Bond Index	0.2
Claymore 1-5 Yr Laddered Government Bond ETF	CLF	Claymore	DEX 1-5 year Laddered Government Bond Index	0
Claymore 1-5 Yr Laddered Government Bond ETF (Advisor Class)	CLF.A	Claymore	DEX 1-5 year Laddered Government Bond Index	-0.1
Claymore Advantaged Canadian Bond ETF	CAB	Claymore	DEX DLUX Capped Bond Index	-0.2
Claymore Advantaged Canadian Bond ETF (Advisor Class)	CAB.A	Claymore	DEX DLUX Capped Bond Index	-0.3
Claymore Advantaged High Yield Bond ETF	CHB	Claymore	Barclays Capital US High Yield Very Liquid index	
Claymore Advantaged High Yield Bond ETF (Advisor Class)	CHB.A	Claymore	Barclays Capital US High Yield Very Liquid index	
Claymore Balanced Growth CorePortfolio ETF	CBN	Claymore	The Sabrient Global Balanced Growth Index	2.9
Claymore Balanced Growth CorePortfolio ETF (Advisor Class)	CBN.A	Claymore	The Sabrient Global Balanced Growth Index	2.7

ETF FUND PERFORMANCE (as of February 28, 2011)				
ETF Name	Ticket	Fund Family	Index	1 Year Return
Claymore Balanced Income CorePortfolio ETF	CBD	Claymore	The Sabrient Global Balanced Income Index	1.9
Claymore Balanced Income CorePortfolio ETF (Advisor Class)	CBD.A	Claymore	The Sabrient Global Balanced Income Index	1.7
Claymore BRIC ETF	CBQ	Claymore	BNY Mellon BRIC Select ADR Index	-1.4
Claymore BRIC ETF (Advisor Class)	CBQ.A	Claymore	BNY Mellon BRIC Select ADR Index	-1.6
Claymore Broad Commodity ETF	CBR	Claymore	Not Applicable	
Claymore Broad Commodity ETF (Advisor Class)	CBR.A	Claymore	Not Applicable	
Claymore Broad Emerging Markets ETF	CWO	Claymore	BNY Mellon BRIC Select ADR Index	-3.6
Claymore Broad Emerging Markets ETF (Advisor Class)	CWO.A	Claymore	BNY Mellon BRIC Select ADR Index	-3.8
Claymore Canadian Financial Monthly Income ETF	FIE.A	Claymore	Not Applicable	5.6
Claymore Canadian Financial Monthly Income ETF - Common	FIE	Claymore	Not Applicable	
Claymore Canadian Fundamental Index ETF	CRQ	Claymore	FTSE RAFI Canada Index	4.9
Claymore Canadian Fundamental Index ETF (Advisor Class)	CRQ.A	Claymore	FTSE RAFI Canada Index	4.8
Claymore China ETF - Advisor	CHI.A	Claymore	Not Applicable	
Claymore China ETF - Common	CHI	Claymore	Not Applicable	
Claymore Equal Weight Banc & Lifeco ETF	CEW	Claymore	Not Applicable	7.5
Claymore Equal Weight Banc & Lifeco ETF (Advisor Class)	CEW.A	Claymore	Not Applicable	7.4
Claymore Global Agriculture ETF	COW	Claymore	MFC Global Agriculture Index	4.9
Claymore Global Agriculture ETF (Advisor Class)	COW.A	Claymore	MFC Global Agriculture Index	4.8
Claymore Global Infrastructure ETF	CIF	Claymore	MFC Global Infrastructure Index	2
Claymore Global Infrastructure ETF (Advisor Class)	CIF.A	Claymore	MFC Global Infrastructure Index	1.8
Claymore Global Monthly Advantaged Dividend ETF	CYH	Claymore	Zacks Global Multi-Asset Income Index	3.6
Claymore Global Monthly Advantaged Dividend ETF (Advisor Class)	CYH.A	Claymore	Zacks Global Multi-Asset Income Index	3.5
Claymore Global Real Estate ETF	CGR	Claymore	Cohen & Steers Global Realty Majors Index	2.5
Claymore Global Real Estate ETF (Advisor Class)	CGR.A	Claymore	Cohen & Steers Global Realty Majors Index	2.4
Claymore Gold Bullion ETF	CGL	Claymore	Not Applicable	0
Claymore International Fundamental Index ETF	CIE	Claymore	The Sabrient Global Balanced Growth Index	5
Claymore International Fundamental Index ETF (Advisor Class)	CIE.A	Claymore	The Sabrient Global Balanced Growth Index	4.8
Claymore Inverse 10 Yr Government Bond ETF	CIB	Claymore	Not Applicable	
Claymore Japan Fundamental Index ETF C$ Hedged	CJP	Claymore	FTSE RAFI Developed ex US 1000 Index	6
Claymore Japan Fundamental Index ETF C$ Hedged (Advisor Class)	CJP.A	Claymore	FTSE RAFI Developed ex US 1000 Index	5.9
Claymore Natural Gas Commodity ETF	GAS	Claymore	NGX Canadian Natural Gas Index	-11.1
Claymore Oil Sands Sector ETF	CLO	Claymore	The Sustainable Oil Sands Sector Index	16.5
Claymore Oil Sands Sector ETF (Advisor Class)	CLO.A	Claymore	The Sustainable Oil Sands Sector Index	16.3
Claymore Premium Money Market ETF	CMR	Claymore	Not Applicable	0.1
Claymore Premium Money Market ETF (Advisor Class)	CMR.A	Claymore	Not Applicable	0.1
Claymore S&P Global Water ETF	CWW	Claymore	S&P Global Water Index	-2.1
Claymore S&P Global Water ETF (Advisor Class)	CWW.A	Claymore	S&P Global Water Index	-2.2
Claymore S&P/TSX Canadian Dividend ETF	CDZ	Claymore	S&P/TSX Canadian Dividend Aristocrats Index	3.7
Claymore S&P/TSX Canadian Dividend ETF (Advisor Class)	CDZ.A	Claymore	S&P/TSX Canadian Dividend Aristocrats Index	3.6
Claymore S&P/TSX CDN Preferred Share ETF	CPD	Claymore	S&P/TSX Preferred Share Index	1.8
Claymore S&P/TSX CDN Preferred Share ETF (Advisor Class)	CPD.A	Claymore	S&P/TSX Preferred Share Index	1.8
Claymore S&P/TSX Global Mining ETF	CMW	Claymore	S&P/TSX Global Mining Index	-3.4
Claymore S&P/TSX Global Mining ETF (Advisor Class)	CMW.A	Claymore	S&P/TSX Global Mining Index	-3.5
Claymore US Fundamental Index ETF - C$ Hedged	CLU	Claymore	FTSE RAFI US 1000 C$ Hedged Index	5.9
Claymore US Fundamental Index ETF - C$ Hedged (Advisor Class)	CLU.A	Claymore	FTSE RAFI US 1000 C$ Hedged Index	5.8
Claymore US Fundamental Index ETF - non-hedged	CLU.C	Claymore	FTSE RAFI US 1000	3.8
Claymore US Fundamental Index ETF - non-hedged (Advisor Class)	CLU.B	Claymore	FTSE RAFI US 1000	3.7
*Horizons AlphaPro Managed S&P/TSX 60 ETF	HAX	AlphaPro Management	S&P/TSX 60 Index	6.1
*Horizons BetaPro COMEX Gold Bullion Bear Plus ETF	HBD	BetaPro Management	COMEX Gold futures contracts	0.7
*Horizons BetaPro COMEX Gold Bullion Bull Plus ETF	HBU	BetaPro Management	COMEX Gold futures contracts	-2.4

ETF FUND PERFORMANCE (as of February 28, 2011)

ETF Name	Ticket	Fund Family	Index	1 Year Return
*Horizons BetaPro COMEX Gold ETF	HUG	BetaPro Management	COMEX Gold futures contracts	-1
*Horizons BetaPro COMEX Silver Bear Plus ETF	HZD	BetaPro Management	COMEX Silver futures contract	-19.8
*Horizons BetaPro COMEX Silver Bull Plus ETF	HZU	BetaPro Management	COMEX Silver futures contract	17.4
*Horizons BetaPro COMEX Silver ETF	HUZ	BetaPro Management	COMEX Silver futures contract	9.2
*Horizons BetaPro MSCI Emerging Markets Bear Plus ETF	HJD	BetaPro Management	MSCI Emerging Markets Index	6.4
*Horizons BetaPro MSCI Emerging Markets Bull Plus ETF	HJU	BetaPro Management	MSCI Emerging Markets Index	-8.5
*Horizons BetaPro NASDAQ-100 Bear Plus ETF	HQD	BetaPro Management	NASDAQ-100 Index	-12.1
*Horizons BetaPro NASDAQ-100 Bull Plus ETF	HQU	BetaPro Management	NASDAQ-100 Index	11.8
*Horizons BetaPro NYMEX Crude Oil Bear Plus ETF	HOD	BetaPro Management	NYMEX Crude Oil futures contracts	-6.5
*Horizons BetaPro NYMEX Crude Oil Bull Plus ETF	HOU	BetaPro Management	NYMEX Crude Oil futures contracts	0.5
*Horizons BetaPro NYMEX Natural Gas Bear Plus ETF	HND	BetaPro Management	NYMEX Natural Gas futures contracts	14.7
*Horizons BetaPro NYMEX Natural Gas Bull Plus ETF	HNU	BetaPro Management	NYMEX Natural Gas futures contracts	-19.9
*Horizons BetaPro S&P 500 Bear Plus ETF	HSD	BetaPro Management	S&P 500 Index	-11.4
*Horizons BetaPro S&P 500 Bull Plus ETF	HSU	BetaPro Management	S&P 500 Index	11.5
*Horizons BetaPro S&P/TSX 60 Bear Plus ETF	HXD	BetaPro Management	S&P/TSX 60 Index	-11.7
*Horizons BetaPro S&P/TSX 60 Bull Plus ETF	HXU	BetaPro Management	S&P/TSX 60 Index	11.8
*Horizons BetaPro S&P/TSX 60 Inverse ETF	HIX	BetaPro Management	S&P/TSX 60 Index	-5.9
*Horizons BetaPro S&P/TSX Capped Energy Bear Plus ETF	HED	BetaPro Management	S&P/TSX Capped Energy Index	-22
*Horizons BetaPro S&P/TSX Capped Energy Bull Plus ETF	HEU	BetaPro Management	S&P/TSX Capped Energy Index	24.9
*Horizons BetaPro S&P/TSX Capped Energy Inverse ETF	HIE	BetaPro Management	S&P/TSX Capped Energy Index	-11.5
*Horizons BetaPro S&P/TSX Capped Financials Bear Plus ETF	HFD	BetaPro Management	S&P/TSX Capped Financials Index	-13.9
*Horizons BetaPro S&P/TSX Capped Financials Bull Plus ETF	HFU	BetaPro Management	S&P/TSX Capped Financials Index	14.9
*Horizons BetaPro S&P/TSX Capped Financials Inverse ETF	HIF	BetaPro Management	S&P/TSX Capped Financials Index	-7.2
*Horizons BetaPro S&P/TSX Global Base Metals Bear Plus ETF	HMD	BetaPro Management	S&P/TSX Global Base Metals Index	2.3
*Horizons BetaPro S&P/TSX Global Base Metals Bull Plus ETF	HMU	BetaPro Management	S&P/TSX Global Base Metals Index	-6.5
*Horizons BetaPro S&P/TSX Global Gold Bear Plus ETF	HGD	BetaPro Management	S&P/TSX Global Gold Index	8.2
*Horizons BetaPro S&P/TSX Global Gold Bull Plus ETF	HGU	BetaPro Management	S&P/TSX Global Gold Index	-12.4
*Horizons BetaPro S&P/TSX Global Gold Inverse ETF	HIG	BetaPro Management	S&P/TSX Global Gold Index	5.6
*Horizons BetaPro US 30-yr Bond Bear Plus ETF	HTD	BetaPro Management	Current Benchmark US 30-year Bond	-0.3
*Horizons BetaPro US 30-yr Bond Bull Plus ETF	HTU	BetaPro Management	Current Benchmark US 30-year Bond	-0.6
*Horizons BetaPro US Dollar Bear Plus ETF	HDD	BetaPro Management	Canadian Dollar in terms of US Dollar	4.8
*Horizons BetaPro US Dollar Bull Plus ETF	HDU	BetaPro Management	Canadian Dollar in terms of US Dollar	-5
*Horizons BetaPro Winter-Term NYMEX Crude Oil ETF	HUC	BetaPro Management	NYMEX light sweet crude oil futures contract	7.2
*Horizons BetaPro Winter-Term NYMEX Natural Gas ETF	HUN	BetaPro Management	NYMEX light sweet crude oil futures contract	-6.6
iShares Alternatives Completion Portfolio Builder Fund	XAL	iShares ETFs	Not Applicable	
iShares CDN Bond Index Fund	XBB	iShares ETFs	DEX Universe Bond Index	
iShares CDN Completion Index Fund	XMD	iShares ETFs	S&P/TSX Completion Index	
iShares CDN Composite Index Fund	XIC	iShares ETFs	S&P/TSX Capped Composite Index	
iShares CDN Corporate Bond Index Fund	XCB	iShares ETFs	DEX All Corporate Bond Index	
iShares CDN Dividend Index Fund	XDV	iShares ETFs	Dow Jones Canada Select Dividend Index	
iShares CDN Energy Index Fund	XEG	iShares ETFs	S&P/TSX Capped Energy Index	
iShares CDN Financials Index Fund	XFN	iShares ETFs	S&P/TSX Capped Financials Index	
iShares CDN Global Gold Index Fund	XGD	iShares ETFs	S&P/TSX Global Gold Index	
iShares CDN Growth Index Fund	XCG	iShares ETFs	Dow Jones Canada Select Growth Index	
iShares CDN Income Trust Index Fund	XTR	iShares ETFs	S&P/TSX Income Trust Index	
iShares CDN Jantzi Social Index Fund	XEN	iShares ETFs	CDN Dow Jones Canada Select Value Index	
iShares CDN LargeCap 60 Index Fund	XIU	iShares ETFs	S&P/TSX 60 Index	
iShares CDN Long Term Bond Index Fund	XLB	iShares ETFs	DEX Long Term Bond Index	
iShares CDN Materials Index Fund	XMA	iShares ETFs	S&P/TSX Capped Materials Index	
iShares CDN MSCI EAFE Hedged to CAD Dollars Index Fund	XIN	iShares ETFs	MSCI EAFE 100% Hedged to CAD Dollars Index	

ETF FUND PERFORMANCE (as of February 28, 2011)

ETF Name	Ticket	Fund Family	Index	1 Year Return
iShares CDN MSCI Emerging Markets Index Fund	XEM	iShares ETFs	MSCI Emerging Markets Index	
iShares CDN MSCI World Index Fund	XWD	iShares ETFs	MSCI World Index	
iShares CDN Real Return Bond Index Fund	XRB	iShares ETFs	DEX Real Return Bond Index	
iShares CDN REIT Index Fund	XRE	iShares ETFs	S&P/TSX Capped REIT Index	
iShares CDN Russell 2000 Index - Canadian Dollar Hedged Index Fund	XSU	iShares ETFs	Russell 2000 Index - Canadian Dollar Hedged	
iShares CDN S&P 500 Hedged to Canadian Dollars Index Fund	XSP	iShares ETFs	S&P 500 Hedged to Canadian Dollars Index	
iShares CDN Short Term Bond Index Fund	XSB	iShares ETFs	DEX Short Term Bond Index	
iShares CDN SmallCap Index Fund	XCS	iShares ETFs	S&P/TSX SmallCap Index	
iShares CDN Tech Sector Index Fund	XIT	iShares ETFs	S&P/TSX Capped Information Technology Index	
iShares CDN Value Index Fund	XCV	iShares ETFs	Dow Jones Canada Select Value Index	
iShares China Index Fund	XCH	iShares ETFs	FTSE/Xinhua China 25 Index	
iShares Conservative Core Portfolio Builder Fund	XCR	iShares ETFs	Not Applicable	
iShares Global Completion Portfolio Builder Fund	XGC	iShares ETFs	Not Applicable	
iShares Government Bond Index Fund	XGB	iShares ETFs	DEX All Government Bond Index	
iShares Growth Core Portfolio Builder Fund	XGR	iShares ETFs	Not Applicable	
iShares MSCI Brazil Index Fund	XBZ	iShares ETFs	MSCI Brazil Index	
iShares S&P CNX Nifty India Index Fund	XID	iShares ETFs	S&P CNX Nifty Index	
iShares S&P Latin America 40 Index Fund	XLA	iShares ETFs	S&P Latin America 40 Index	
iShares US High Yield Bond CAD-Hedged Index Fund	XHY	iShares ETFs	Markit iBoxx USD Liquid High Yield Index	
iShares US IG Corporate Bond CAD-Hedged Index Fund	XIG	iShares ETFs	Markit iBoxx USD Liquid Investment Grade Index	

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ETF Spotlight

Global X Funds Launches First ETF Focused On Canada's TSX Venture Exchange

New York - March 17, 2011 - Global X Funds, the New York based provider of exchange traded funds (ETFs), today launched the Global X S&P/TSX Venture 30 Canada ETF (Ticker: TSXV). This is the first ETF globally targeting companies on Canada's junior exchange, the TSX Venture, for emerging companies.

TSXV provides investors with a wide range of commodity exposure via exploration and junior mining companies listed on the TSX Venture Exchange. The fund also may benefit from continued demand for commodities from fast-growing emerging market countries combined with the quantitative easing policy in the US. These particular companies have low production costs, making them prime acquisition targets for larger companies that are suffering from depleting commodity reserves (NASDAQ 2010).

"We are pleased to provide the first vehicle that easily tracks the S&P/TSX Venture 30 Index," said Bruno del Ama, ceo of Global X Funds. "Our innovative product allows investors access to a previously difficult to trade, illiquid market."

The Global X S&P/TSX Venture 30 Canada ETF tracks the S&P/TSX Venture 30 Index, which seeks to measure the performance of 30 of the largest and most liquid securities listed on the TSX Venture Exchange. As of March 14, 2011, the three largest components of the index were Atac Resources Ltd, Canacol Energy Ltd, and Rainy River Resources Ltd.

About Global X Funds
Global X Funds is a New York-based provider of exchange-traded funds that facilitates access to investment opportunities across the global markets. With over $1.5 billion in managed assets as of March 1, 2011, it is one of the fastest growing ETF providers in the world with a focus on Global Commodities, Developed and Emerging Markets fund suites. For more information, please visit **www.globalxfunds.com**

Announcements

Hillsdale Proudly Announces the Winner of the Toronto CFA Society & Hillsdale Canadian Investment Research Award

Pauline Shum Announced as Winner of Inaugural Toronto CFA Society Hillsdale Research Award.

Toronto CFA Society is happy to announce that Dr. Pauline Shum is the first recipient of their newest award, the Toronto CFA Society & Hillsdale Canadian Investment Research Award, for her research paper entitled “The Long and Short of Leveraged ETFs: the Financial Crisis and Performance Attribution.”

Visit **http://www.hillsdaleinv.com/news/Shum_Leveraged_ETFs.pdf** to download the Award Winning Research Paper in PDF format.

"Professor Shum's paper provides an extremely useful framework for practitioners to use in their analysis of ETFs,” according to Chris Guthrie, CFA, President & CEO, Senior Portfolio Manager and Founding Partner, Hillsdale Investment Management Inc. He went on to say that:

“Ms. Shum has disaggregated the relative performance of ETFs into three distinct components, namely the compounding effect of hold periods of more than one day, the managers' effectiveness and costs of achieving their objectives, particularly across multiple time periods, and lastly, the efficiency of ETFs in maintaining a small premium or discount to NAV. Pauline's paper was chosen from among 15 high quality submissions for the Toronto CFA Hillsdale Research Award, proof that Toronto CFA Society’s and Hillsdale's objective of supporting high quality investment research is being met. Congratulations to Peter Jarvis, CFA, Executive Director of Toronto CFA Society and to Harry Marmer, CFA, Executive Vice President of Hillsdale Investment Management Inc., for establishing this award. Hillsdale looks forward to next year's submissions with great anticipation.”

Research Papers are judged on the potential contribution of their applied research to topics of interest related to Canadian capital markets. Areas of interest include any aspect of investment management, such as portfolio management, asset valuation, risk management, compliance and performance evaluation. Investment fields include traditional and alternative investments, as well as all asset classes and investment vehicles (e.g., fixed income, equities, derivatives, etc.). The winner, which was announced at a Toronto CFA Society Awards Reception on March 3rd, received a research award of $10,000 CAD.

Award winner, Pauline Shum, reflected: “I am thrilled to be the winner of the inaugural Toronto CFA Hillsdale research award. It is an honour for my work to be recognized by renowned professionals in the field”.

Hillsdale Investment Management
Founded in 1996, Hillsdale is a leading Canadian independent investment boutique, providing a full range of traditional equity and alternative investment strategies to both institutional and individual investors. Hillsdale manages a spectrum of long only, long/short and custom designed strategies employing a core investment style carefully implemented using an adaptive multi-strategy, risk controlled process.

Pauline Shum
Pauline Shum (BA (Hons), MA, PhD) is a finance professor at the Schulich School of Business, York University, where she has taught at the BBA, MBA, PhD, and executive levels. Prof. Shum was the Director of the PhD program in Administration from 2001 to 2005, and is the Founding Director of the Master of Finance (MF) program, launched in August 2009. Prof. Shum's financial research has appeared in numerous international academic and professional outlets as well as conferences. Prof. Shum serves on the investment committee of the York University Pension Plan; she is also an experienced economic consultant.

Toronto CFA Society
Toronto CFA Society is a not-for-profit organization supporting the professional and business development of CFA charterholders. The society provides members with a local perspective on a global designation including: educational programs, sponsored events, job postings, quarterly newsletters, a comprehensive affinity program and networking opportunities.

Celebrating its 75th anniversary in 2011, the society is affiliated with CFA Institute, the global body that administers the Chartered Financial Analyst curriculum and sets voluntary, ethics-based performance-reporting standards for the investment industry. With over 7,300 members, Toronto CFA Society is the 2nd largest in the world. Our members are leaders in ethics within the financial community. For more information, please refer to **www.torontocfa.ca.**

For Further Information:

Hillsdale Investment Management Inc.
Harry Marmer
Executive Vice President, Institutional Investment Services
Phone: 416-913-3907
hmarmer@hillsdaleinv.com

Toronto CFA Society
Sara Maginn Pacella
Manager External Communication & Member Services
Phone: 416-366-5755 x 225
spacella@torontocfa.ca