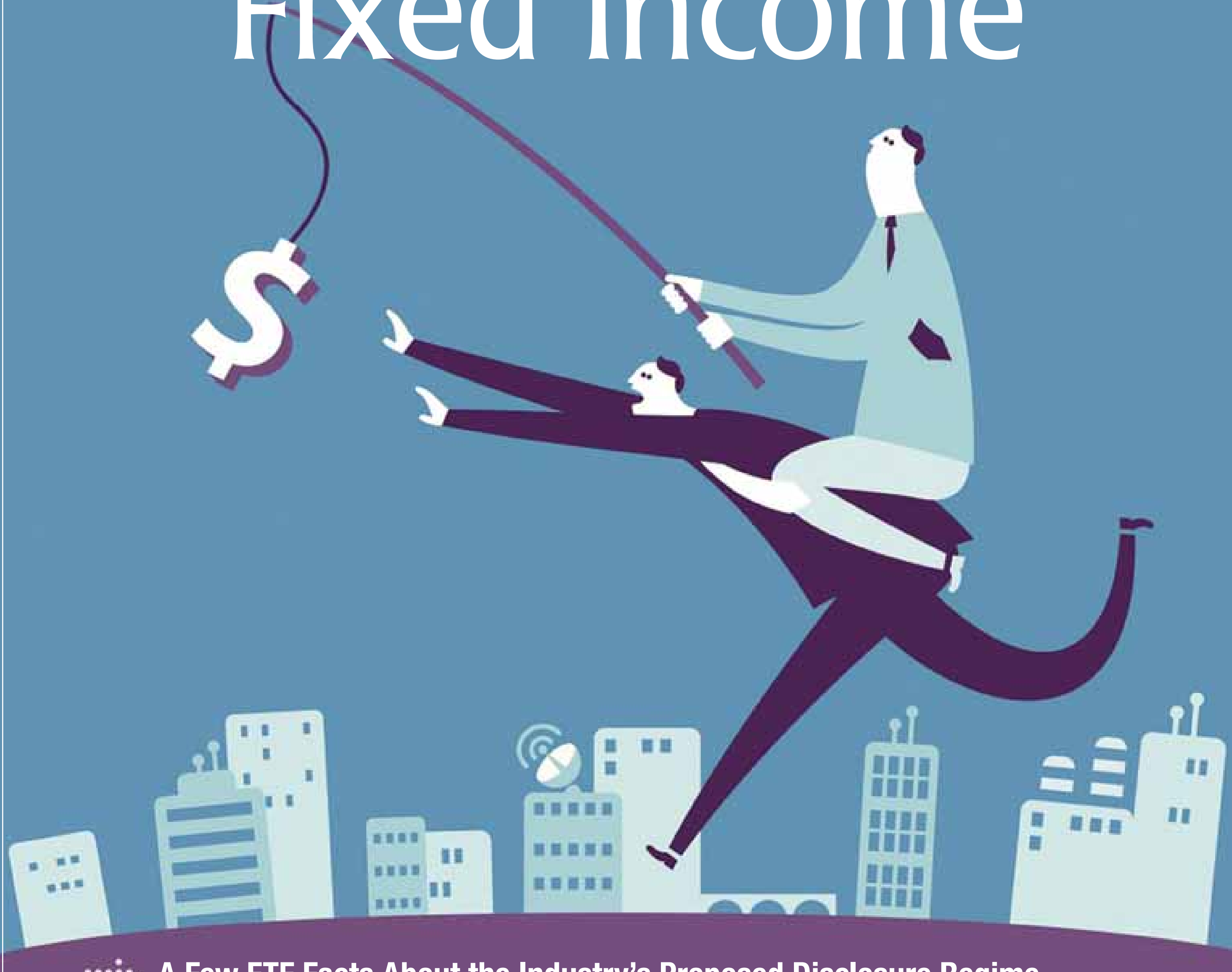
CANADIAN ETF Watch
VOL 6 ISSUE 4 JULY 2015
canadianetfwatch.com

Stripping Away Preconceived Notions of Fixed Income



- A Few ETF Facts About the Industry's Proposed Disclosure Regime
- ETF Toronto Conference Review

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Assets invested in ETFs/ETPs listed in Canada increased 2.6% in the first half of 2015 according to ETFGI

Assets invested in ETFs/ETPs listed in Canada increased 2.6% in the first half of 2015, according to ETFGI's preliminary ETF and ETP global insights report for the first half of 2015. At the end of June 2015, the Canadian ETF industry had 367 ETFs, with 521 listings, assets of US$68 Bn, from 11 providers listed on 1 exchange.

"June was a difficult month for most markets around the world. The S&P 500 index ended June down 2% for the month and finished the first half of 2015 up 1%. Market performance in the first half of 2015 was impacted by a number of uncertainties in the first half of 2015: the situation in Greece and the impact on the Eurozone, when the Fed will raise interest rates, volatility in the Chinese market and the MERS outbreak in South Korea." according to Deborah Fuhr, managing partner of ETFGI.

In the first half of 2015 record levels of net new assets (NNA) have been gathered by ETFs/ETPs listed globally with US$152 billion beating the prior record of US$130 billion in the first half of 2014. US listed ETFs/ETPs gathered US$103 billion, beating the previous record of US$76 billion gathered in the first half of 2012, ETFs/ETPs in Japan gathered US$18 billion beating the prior record of US$13.5 billion set in the first half of 2014, and European listed ETFs/ETPs gathered US$40 billion, beating the US$32 billion gathered in the first half of 2014.

In June 2015, ETFs/ETPs listed in Canada gathered net inflows of US$984 Mn. Equity ETFs/ETPs gathered the largest net inflows with US$814 Mn, followed by fixed income ETFs/ETPs with US$85 Mn, and commodity ETFs/ETPs with US$20 Mn.

Year to date (YTD) through end of June 2015, ETFs/ETPs have seen net inflows of US$6.6 Bn. Equity ETFs/ETPs gathered the largest net inflows YTD with US$3.1 Bn, followed by fixed income ETFs/ETPs with US$2.6 Bn, while commodity ETFs/ETPs suffered net outflows of US$17 Mn.

Source: www.etfgi.com

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CANADIAN ETF Watch
canadianetfwatch.com
JULY 2015 | VOL. 06 NO. 04

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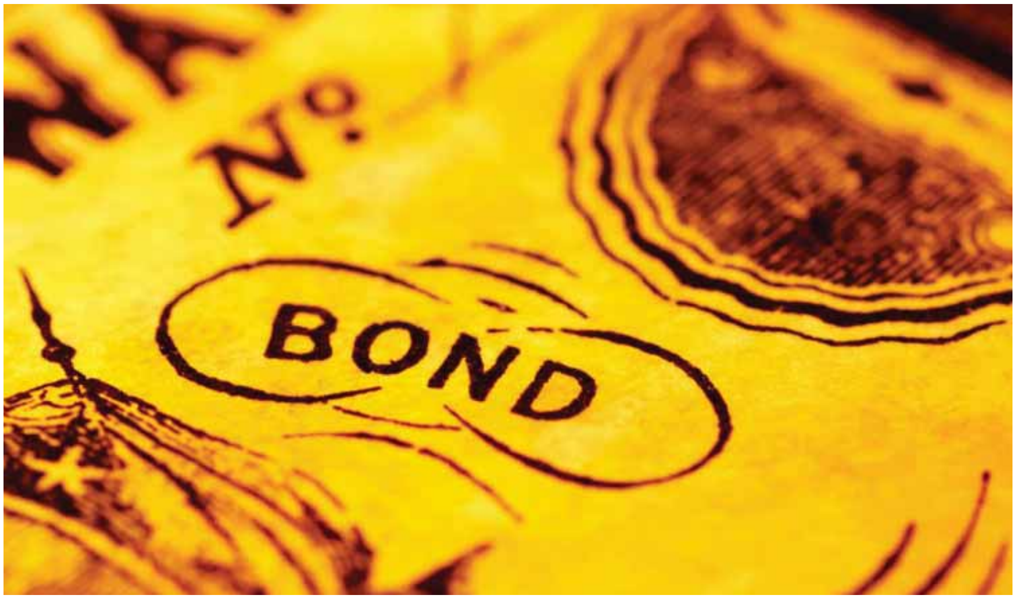

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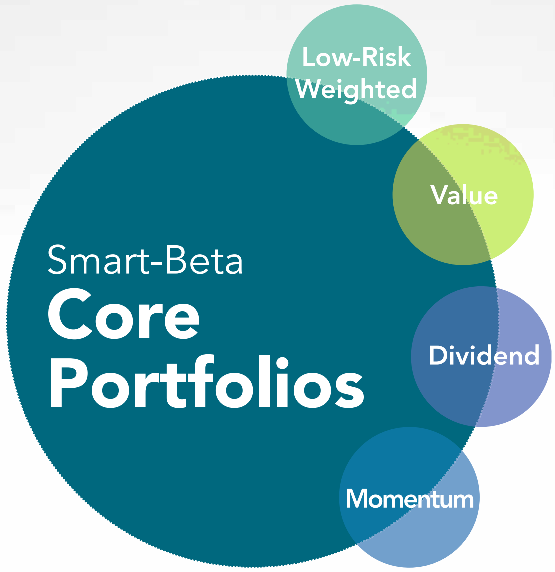
CHANGING ETF INVESTING



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	ETF Information		
NEW ETFs	TSX:CBB	First Asset Core Balanced ETF	
NEW ETFs	TSX:CED	First Asset Core Canadian Equity ETF	
NEW ETFs	TSX:CES	First Asset Core U.S. Equity ETF	Hedged Units
NEW ETFs	TSX:CES.B	First Asset Core U.S. Equity ETF	Unhedged Units
NEW ETFs	TSX:CES.U	First Asset Core U.S. Equity ETF	U.S. $ Units

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[1]Source: Morningstar.

Stripping Away Preconceived Notions of Fixed Income

Without question, bond investors over the past few decades have done quite well for themselves, enjoying the tailwinds afforded them by a prolonged period of declining interest rates.

John Pagliacci
Product Strategist, First Asset Exchange Traded Funds

So far in 2015, the Bank of Canada has cut interest rates twice (in January and July). While it's unclear as to whether or not the Bank of Canada will decide to cut interest rates again later this year, it's likely safe to say that Canada is in the 9th inning of this trend.

Unfortunately, because bond returns have been so good for so long, the fear is that Canadians have become complacent with their bond portfolios, expecting to maintain a similar performance profile while continuing to earn ample income. But more active market participants will likely realize that today's bond environment is much more challenging, and much more difficult to meet expectations, both from a total return as well as an income perspective. As a result, it's probably a prudent idea to reassess what sort of bond exposure Canadians have in their fixed income portfolios.

With Canada's aging population, bonds are an increasingly important component of overall investment portfolios, as seniors typically become more conservative with their investments in retirement. Yet, what isn't likely immediately clear to investors is that not all bonds are created equal, and some of these allocations to bonds historically seen as 'safe' are potentially exposing investors to unintended risks.

Shorter duration: Strategically sound in this environment

Take for example the FTSE TMX Canada Universe Bond Index, the broadest and most widely used proxy for Canadian investment grade government and corporate bonds. As of June 30, 2015, the duration of this index was roughly 7.5. For those less familiar with the term, duration is a measure of the sensitivity of bond prices as interest rates move; and the bigger the duration number the greater the interest rate risk/reward for bond prices. Take, for example, an instance over the past 30 years where interest rates fell by 1%. A duration of 7.5 would indicate, all else being equal, that the bond's price would increase by roughly 7.5%, a handsome return indeed. However, the reverse of that is also true, if interest rates were to rise by 1%, the price of that bond would decline by 7.5%. While we don't envision interest rates rising by 1% any time in the very near future, we do believe that we're getting closer to an inflection point where we transition from declining interest rates to increasing interest rates over time. Therefore, to mitigate interest rate risk, choosing shorter duration investments (bonds that mature sooner rather than later) is a sound strategy.

With greater yield comes greater risk

Another unintended risk of maintaining a 'status-quo' bond portfolio is that, because interest rates are so low, bond yields are quite depressed. To combat this and earn more income, some investors have simply been chasing after products that offer higher yield without being fully aware of exactly what they're buying into. For instance, generally speaking, higher yields typically come from taking on either more credit risk (the risk of the bond issuer not being able to repay its debt) or more duration risk (having to wait longer for a bond to mature and, hence, being more exposed to changing interest rates). Thus, higher yield does not simply equate to better performance.

Tax rates differ and not all fixed income is inefficient

Lastly, while not a 'risk', per se, investors perhaps haven't necessarily focused as much as they should on the tax efficiency of their fixed income investments. Being that interest income is taxed at the highest applicable rate, minimizing the amount owed to the government can, and does, go a long way in enhancing overall returns on bond investments.

A solution for bond risks and a solid plan for investor needs

Recognizing these very real risks and needs facing Canadian bond investors, in June of 2013 First Asset launched an ETF that invests in strip bonds derived from Canadian federal and provincial government issues, the First Asset 1-5 Year Laddered Government Strip Bond Index ETF (TSX: BXF) ("BXF" or the "Fund"). Government bonds afford the portfolio a credit risk that is essentially zero. Strip bonds are a fixed- income product that, as their name implies, are stripped of the coupon and pay no interest throughout their term. They are purchased at a discount and mature at par. In the BXF portfolio the strip bonds are equally weighted to mature in tranches between 1-5 years, which makes it an ideal solution for those looking to mitigate interest rate risk. Also, because strip bonds trade at discounts to their par values and pay no interest, investors benefit from significant tax efficiency, allowing more of their returns to remain in their pocket, as exemplified below. As you can see, the strip bond investor in our hypothetical example would end up with a considerably higher after-tax return than if they invested in a Government of Canada (GOC) premium bond.

	GOC premium bond	Strip bond
Term to maturity	3 years	3 years
Coupon	4.25%	0.00%
Yield to maturity	0.60%	0.60%
Initial investment	$100,000	$100,000
Bond Price	$110.84	$98.22
Maturity Value	$90,218	$101,813
Calculations		
Initial investment/outlay	($100,000)	($100,000)
+ Interest Received	$11,503	$0
+ Maturity Value	$90,218	$101,813
= Gross Return	$1,720	$1,813
- Tax Payable	($5,176)	($816)
= Net Return	**($3,456)**	**$997**

Hypothetical example for illustrative purposes only.

Continued on page 8

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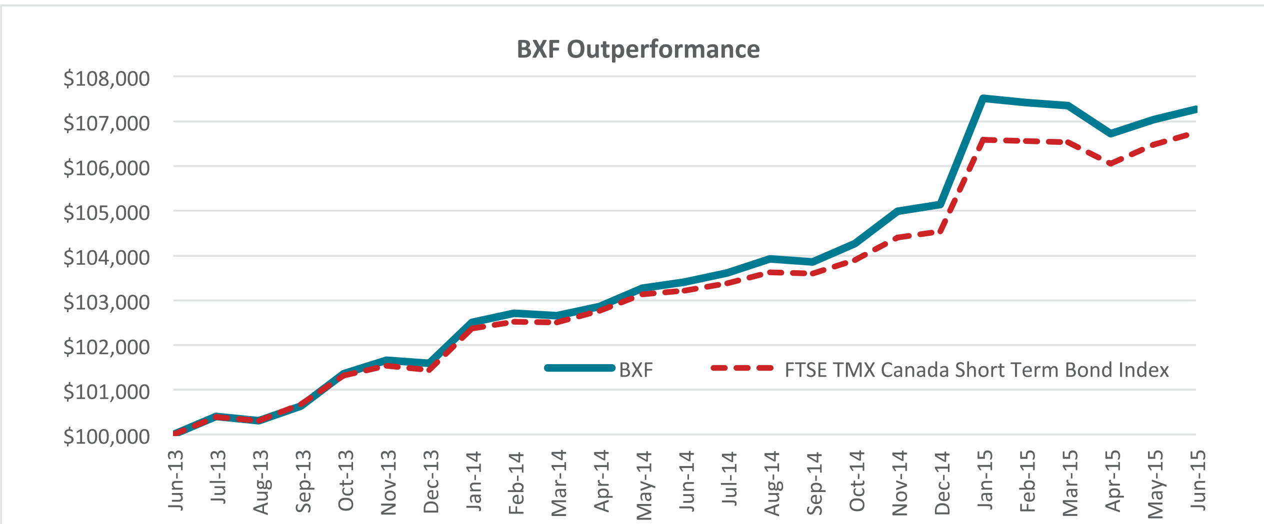
Despite strip bonds not paying out any interest, BXF is structured in such a way that quarterly distributions are in fact paid to unitholders, in amounts based on the portfolio holding's average yield to maturity, funded by small cash balances held within the ETF. So income seeking investors need not worry about an absence of cash flow.

Whether you're concerned about your portfolio's tax inefficiency, credit risk, interest rate risk, or a combination of all three, BXF is certainly worth considering, particularly since it's been the best performing short-term government bond fund, both on a before-tax and after-tax basis, dating back to its inception date.

Performance as at June 30, 2015	**1 year**	**2 year**	**Since Inception[2]**
First Asset 1-5 Year Laddered Government Strip Bond Index ETF (BXF)	3.74	3.57	3.28



Source: Morningstar Direct. As at June 30, 2015.

The rate of return chart shown is used only to illustrate the effects of the compound growth rate and is not intended to reflect future values of the Index or the Fund or returns on investment in the Fund.

The FTSE TMX Canada Short Term Bond Index is a market capitalization weighted index consisting of a broadly diversified range of investment grade federal, provincial, municipal and corporate bonds with a term to maturity between one and five years. The Index is used as a benchmark to help you understand the Fund's performance relative to the general performance of Canadian short-term bonds.

1. Source: Morningstar Direct as at June 30, 2015: BXF was the top performing government bond ETF versus other government bond ETFs in the Canadian Short-Term Fixed Income category for exchange traded funds, which has 21 ETF funds in the category. The Morningstar performance ranking is solely based on total return performance since BXF's first day of trading on June 11, 2013. The Fund's performance is subject to change every month.

2. Inception Date of BXF is June 5, 2013

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John Pagliacci, Product Strategist, First Asset Exchange Traded Funds jpagliacci@firstasset.com

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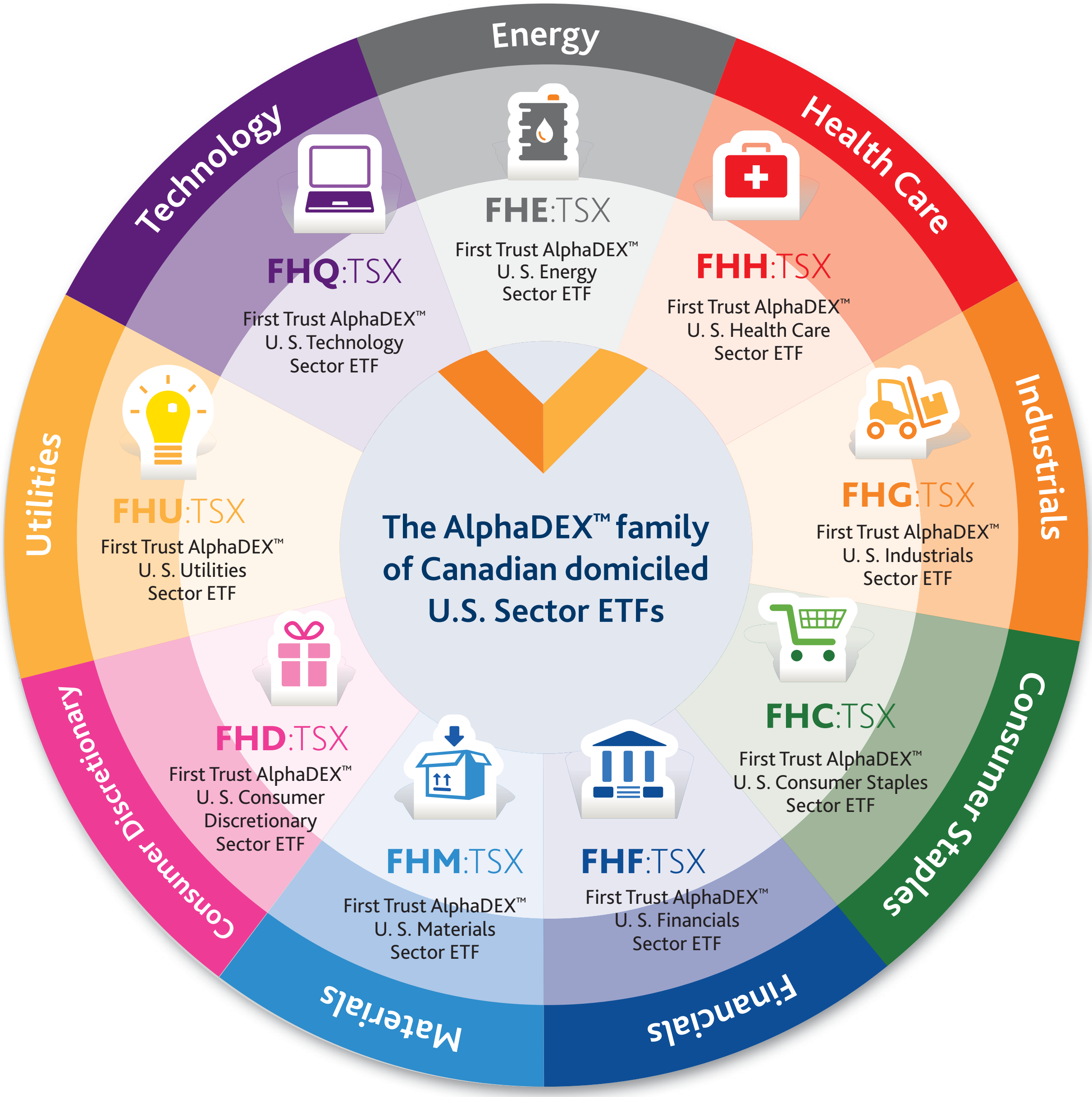

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A Few ETF Facts About the Industry's Proposed Disclosure Regime

The Canadian securities regulators recently proposed rule changes that would codify a summary disclosure document for ETFs (referred to as ETF Facts) and the manner in which ETF offering documents are to be delivered to investors.

Kevin Rusli
Partner
Blake, Cassels & Graydon LLP

The regulatory evolution of the ETF Facts in Canada mirrors the U.S. experience, which implemented their own version of an ETF Facts in 2009. In both instances, the starting point for the content of the ETF Facts was the summary disclosure document already in use for conventional mutual funds (in Canada, this mutual fund summary document is referred to as Fund Facts), which by its own accord, was already subject to extensive regulatory research, consultation and investor testing.

In both Canada and the U.S., a primary objective of the ETF Facts was to exclude the legalese that had become customary of lengthy prospectuses and to replace that with a more investor-friendly (no more than four pages in length) executive summary.

At a high level, the proposed ETF Facts serve to (i) bridge the information gap that has been identified between participants in the ETF industry and retail investors, and (ii) level the playing field with mutual funds by adopting standardized offering documents and harmonizing the disclosure regime. Using the Fund Facts as the initial canvass, the proposed ETF Facts have been modified to address the market distribution model underlying the ETF structure. In a nutshell, unlike a mutual fund which can be purchased or redeemed directly with the fund, individual investors of ETFs (like you and I) typically purchase and sell ETF securities over the secondary market. As a result, you will not find information pertaining to purchases and redemptions that are made directly with the fund in the ETF Facts, which are generally limited to market makers or major financial institutions. Instead, the ETF Facts have been specifically designed to help investors and advisors find key information they need to make informed investing decisions.

Blakes
LAWYERS

Based on significant research on ways to improve ETF Facts for the benefit of investors, the regulators conducted several in-person interviews and online surveys, and learned that many investors lacked an in-depth understanding of certain key information that could be considered important to making an informed decision. The research also reconfirmed that investors prefer to receive a concise summary of key information, rather than a prospectus that may contain overwhelming or complicated disclosure (which often includes information pertaining to funds that are not being considered by the investor). Specifically relating to the ETF distribution model, it was evident that investors needed additional guidance to better understand certain basic secondary market terminology, such as bid-ask spreads, premiums and discounts and the relationship between market price and net asset value. These are concepts that would generally be foreign to an investor who only bought and sold conventional mutual funds. The solution to filling in this education gap was to provide plain language explanations in the ETF Facts, with the hope that the new content on trading and liquidity would provide investors with enough insight with which to make an educated decision. If all goes according to plan, the industry will benefit from a tailored disclosure document prescribed by law that will educate investors about the benefits, risks, costs, and objectives of various ETFs, all within an accessible, plain language and comparable format. In effect, investors will receive a simplified version of key prospectus information, without compromising the quality of disclosure.

As part of the third stage of the Canadian Securities Administrator's point of sale disclosure project, one that will generally require Fund Facts to be delivered to investors of conventional mutual funds before the point of sale (i.e. pre-trade) commencing on May 30, 2016, the proposed rule changes also introduce a new prospectus delivery regime for ETFs. Under the proposed regime, dealers that receive purchase orders for ETFs will be required to deliver the ETF Facts (rather than a prospectus) to investors within two days of purchase. From a securities law perspective, the proposed delivery requirement shifts the onus of delivery from the dealer on the sell-side (e.g. the underwriter in an ETF distribution) to the dealer when acting as agent of a purchaser (the "buy" side).

The ETF Facts and new delivery regime effectively codify material elements of prior granted exemptive relief provided to ETF managers and dealers back in the Fall of 2013. In summary, it is proposed that all investors receive key information provided in a concise manner, that if consumed, will lower the risk of investors buying inappropriate products, put investors and advisors in a better position to compare products, provide greater transparency around commissions and costs of investing and overall, reinforce investor confidence in the ETF industry. The proposed amendments are available for comment until September 16, 2015.

Kevin Rusli, Partner, Blake, Cassels & Graydon LLP
kevin.rusli@blakes.com

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EXCHANGE TRADED FORUM 2015

Tuesday, May 26 & Wednesday, May 27

One King Street West

Toronto Conference Review

Women in ETFs (WE) Presented: The ETF Network – Delivering ETF Strategies to the Customer

Back row: Ling Zhang, Aye Soe, Linda Zhang, Deborah Fuhr
Front row: Moderator, Deborah Frame, Oricia Smith, Sharon French

*The Exchange Traded Forum, Toronto, was created by **Radius Financial Education (Radius)** and brought together leading professionals from every segment of this dynamic group of investment providers including investors, advisors, managers, research professionals, regulatory experts and noted financial educators, to review the past, assess the present and discuss strategic options for achieving continued future success.*

Recent years have shown exponential growth and change in Exchange Traded Products. Building a top down agenda allowed us to focus on educating our attendees on the role Canada has played in this growth, the current trends around the world and the economic environment, rising interest rates, regulatory changes, building better portfolios, Exchange Traded Receipts and issues financial advisors are facing today. Our distinguished list of speakers, each an authority in their field, did just that!

Radius' goal is to host a truly educational forum and we would like to thank our speakers and sponsors for their invaluable contribution. We would also like to thank all those who completed an evaluation form as these comments are essential and will be the foundation for our **2016 ETF Forums**.

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Deborah Fuhr, ETFGI

Pat Bolland, Media Consultant

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Trevor Cummings,
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Tyler Mordy,
HAHN Investment Stewards

Warren Jestin, Scotiabank

Rick Ferri, Portfolio Solutions

Fiona Wilson, Guardian Capital LP

Amanda Davidson, BMO Capital Markets

The surging popularity of exchange-traded funds (ETFs) is creating an investment culture in which both large and small investors are focusing more on asset allocation than the quality of individual securities, according to two ETF experts who delivered a keynote speech at the **2015 Exchange Traded Forum** in Toronto on Wednesday, May 26.

"When large investors hit the panic button, either up or down, they focus on asset classes and not on individual stocks," **Matt Hougan**, CEO of New York-based education and research firm **ETF.com** told the conference in a joint keynote address with **David Nadig**, director, ETFs, with Norwalk, Conn.-based financial data provider FactSet Research Systems Inc.

"When something big happens and it's time to buy, they focus on asset classes, and it's the same when something goes wrong and it's time to sell," Hougan added. *"As a result, the correlation of individual stock movements has been rising for years."*

At the same time, the advent of commissions-free or low-commissions trades in ETFs has made retail a massive market for ETFs in the U.S. as investors appreciate their low management fees, transparency and liquidity. In fact, ETFs account for as much as 25% of trading on the New York Stock Exchange on some days, Hougan said.

Correlation in stock movements on an exchange can be as high as 80%-90% in panic times, Nadig added, and the trend is being aggravated by high-volume, high-frequency traders focusing on short-term trades.

"When things get hairy, everyone moves in one direction and individual stock-picking is getting harder," he said. "In addition, high-frequency traders are now playing the ETF game. It's like robbing banks. They go where the money is."

ETFs have *"flattened the investment landscape,"* giving ordinary retail investors access to globally diversified portfolios with rock-bottom management fees that would have been accessible to only a few privileged institutional investors a decade ago, Hougan said. As well, more than half of institutional managers are using ETFs for both core and satellite strategies.

"The core benefits of ETFs are easily understood, but there is more disruption coming," Nadig said. *"This is only the pointy end of the hockey stick right now."*

Specifically, automated asset-allocation programs and robo-advisors are providing investors with simple tools that help them assemble customized and diversified asset mixes, essentially creating mass access to portfolio building techniques. Thus, investors don't have to be particularly smart to assemble massively diversified global investment portfolios using ETFs, Nadig said, with the easy accessibility and liquidity the product offers.

"You can fire and forget with these automated programs and simply rebalance your portfolio once a year," Nadig said. "Investors get a stellar experience for almost no money. The allocation process has become so simple a robot could do it – and robots are in fact doing it."

Robo-advisors are on the rise, and the inexpensive allocation services they provide threaten the value of asset-allocation advice that individual financial advisors offer, said Hougan.

"We see big challenges ahead for advisors, and yelling at the cloud isn't going to make it go away," he said.

As a result, advisors may have a hard time providing value and charging fees for advice in securities selection and asset allocation as a result of these innovations, Hougan said.

However, you can add value by becoming a *"network advisor"* in which you offer clients access to professional advice in the areas of estate planning, legal or taxes. In some cases, it may make sense to bring qualified experts into your practice.

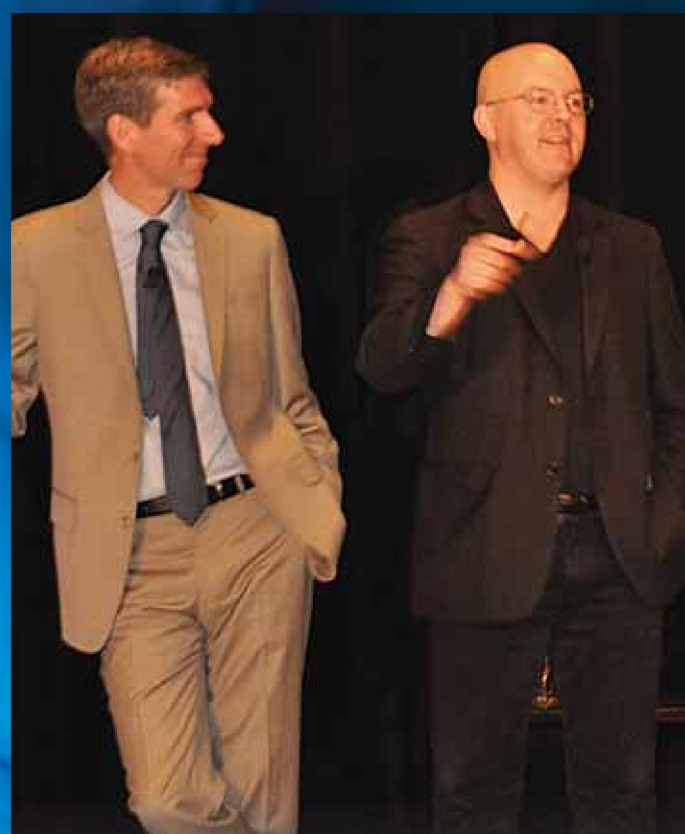
Another option is to incorporate robo-advisors or automated investment services into your practice, increasing the size of your client base to make up for the fact that you may have to become more competitive on fees.

"It's difficult to import a lot of high net-worth clients, but the robo-advisor approach allows you to bring clients onboard you wouldn't normally touch and simply offer them model portfolios," Nadig said. *"You need more clients at low fees to succeed in the automated world, but some of these low net-worth clients will eventually become high net-worth."*

If you are particularly skilled at asset allocation and securities selection, you can also differentiate yourself as a portfolio manager or ETF strategist, and clients will pay for your services, Hougan said. Nevertheless, Hougan wouldn't be surprised to see U.S. technology giants such as Google Inc. or Amazon.com Inc. enter the financial services business as it becomes more automated – and that would be *"transformational"* for the investment industry.

These firms are experts at gathering specific information on the tastes and purchases of individual clients and they would be able to provide services targeting their needs, he said. The huge scale of their business reach could drive fees down even further for financial services.

Coverage courtesy of Investment Executive.
www.investmentexecutive.com.


Matt Hougan, ETF.com Dave Nadig, FactSet

It's an exciting time to be a bond ETF investor, according to an expert panel that presented at the 6th annual Exchange Traded Forum in Toronto.

That panel, which outlined how to rethink bond investment strategies, included **Scott Boniferro**, product manager at Invesco Canada; **Barry Gordon**, president and CEO of First Asset; **Alfred Lee**, vice president and portfolio manager at BMO ETFs; and **Daniel Straus** of National Bank Financial, as moderator.

For more on why and how to incorporate bond ETFs in clients' portfolios, check out deputy editor **Melissa Shin**'s live tweets below.

Scott Boniferro, Invesco Canada

Barry Gordon, First Asset

Alfred Lee, BMO ETFs

Daniel Straus, National Bank Financial

Live tweets from the 6th Annual ETF Forum Toronto

It's an exciting time to be a bond ETF investor. There are 100 such ETFs in Canada, and there have been $3 billion in flows over the last few years **@radiusfe @advisorca**

Do real opportunities still exist in bonds? Boniferro says it's time to diversify, and to think of interest rates and credit risk. **@advisorca @RadiusFE**

The high-yield, senior-secured and preferred-share markets all offer better yield, says Boniferro **@advisorca @RadiusFE**

Gordon says to look at tax efficiency of products and consider asset location **@advisorca @RadiusFE**

Having both floating-rate and longer-duration strategies in one product is good, says Gordon. That allows for diversification. Also consider active management.

Lee: The Canadian universe has limited opportunities: average duration of bond ETFs is 7.5, and average yield 2%. ETFs allow investors to get in and out of the market as needed **@advisorca**

Lee: manage risk. Choose short duration bonds, not because interest rates will rise — in fact, he says, rates will be low for awhile. But uncertainty in interest rates means it's good to have short durations. To make up for short durations, overweight credit to make up yield.

Policy divergence globally is going to help bond markets, adds Lee **@advisorca @RadiusFE**

Bonds are tax-inefficient. If a bond has a premium, and YTM lower, the yield is lower than tax rate.

You have a lot of premium bonds with negative after-tax yields. By choosing short durations, you'll choose a limited number of premium bonds **@advisorca @RadiusFE**

Floating-rate bonds can be tax-efficient, says Boniferro. Their tax liability matches their value. High-yield and floating-rate bonds are also more tax-efficient.

Gordon: use a laddered approach with strip bonds. They accrete to par. Their YTM = current yield, so they're more tax-efficient. They're usually low duration, too

Lee: Can buy bonds that trade at discount, so the YTM is higher than coupon. That's more tax-efficient.

Bond ETFs can be more liquid than securities themselves in times of panic, during which people use ETFs for price discovery, says Boniferro **@advisorca**

Gordon: mismatch in crisis when ETF more liquid than underlying is concerning.

Gordon: People think the secondary market is reflective of liquidity, but it can dry up in a crisis. You could be stuck with primary market liquidity only.

Boniferro: ETF helps you spread your risk due to diversity. Market makers will provide liquidity in a no-bid situation. You may have higher spreads and not get best execution, but the ETF market maker will come up with a price, says Boniferro.

Check out the rest of the tweets at **twitter.com/melissagshin.**

Coverage courtesy of Advisor.ca

ETF Announcement

Auspice launches the world's first Canadian Crude Oil ETF

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Auspice launches the world's first ETF based on Canadian Crude Oil

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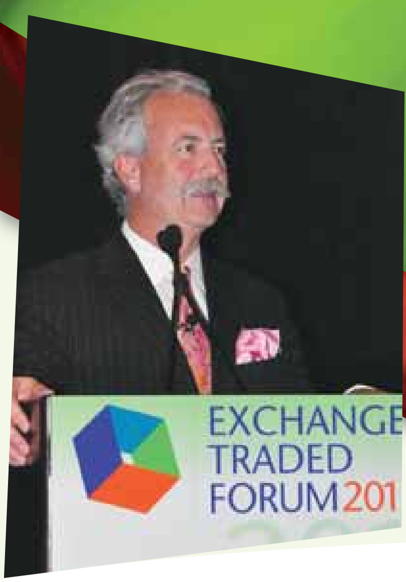

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