Global Asset Management

RBC Exchange Traded Funds

How to use ETFs in a portfolio

ETFs are flexible investment and trading vehicles that can be used within a portfolio in many ways to meet different investment needs and objectives.

1 Diversification

The immense complexity of global markets calls for an active and effective asset-allocation strategy to preserve and grow wealth. Various approaches can be taken using ETFs to deliver diversified market exposure and active market participation.

a. Buy-and-hold investing

An investor can use a portfolio of ETFs to achieve a strategic asset allocation based on time horizon, financial objectives and risk appetite. Periodic rebalancing can help maintain the portfolio's original allocation or, the allocation can be incrementally changed to become more conservative over time as the investment horizon nears.

An investor can build a well-diversified ETF portfolio with exposure to various asset classes, investing styles and geographic regions. The relatively low cost of ETFs can help maximize net returns.

b. 'Core-and-satellite' investing

A core-and-satellite strategy starts with building the core of the portfolio with ETFs that provide broad market exposure, including allocations to fixed income and equities. The core portion can serve as the long-term anchor of the portfolio delivering market performance and provide a sense of stability.

The other, more tactical 'satellite' portion of the portfolio can be used to express a view or take advantage of perceived market opportunities through access to specific industries, sectors, styles, regions, commodities, or even macroeconomic trends. Investors can effectively use ETFs to express their views and complement the core holdings in their portfolio.

c. Thematic or tactical investing

ETFs can be used within a portfolio to make short-term tactical adjustments to the asset mix to over- or under-weight certain styles, regions or industries, without having to invest in individual securities. This allows investors to respond to overall macro ideas while avoiding security-specific risks.

2 Cash equitization

Cash equitization means investing a cash position to maintain desired market exposure over the short term before a longer-term position is purchased. The broad market exposure, liquidity and relatively low cost of ETFs make them an ideal vehicle for cash equitization.

Related to cash equitization is **transition management** – When investors change asset managers or investment solutions, there may be a need to preserve the exposure during the period between exiting the old solution and investing in the new solution. An ETF can act as an excellent temporary vehicle to maintain the asset allocation and required investment exposure during this transition period. When the new investment solution is identified, the ETF can be sold, with the proceeds invested in the new solution.

3 Tax management

ETFs can be used to facilitate a number of tax management strategies. For example, you may wish to sell a security to trigger a capital loss to offset capital gains realized during the current year or previous three years (they can also be carried forward). When triggering a capital loss, you are not allowed to deduct the loss if you purchase an identical security to the one sold within 30 days of settlement date. By purchasing an ETF, you can maintain your exposure to the sector or market that the sold securities represent.

About RBC Global Asset Management

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