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ETFs popular but be careful when you invest

Examining some of the specialty ETFs on the market

Exchange-traded funds (ETFs) continue their rising popularity. The ETF Industry Association reports that U.S.-listed ETFs account for $1.2 trillion in assets under administration as of the end of February. That's a 14% increase on a year-over-year basis.

There are good reasons that investors are drawn to ETFs. They offer trading flexibility, transparency, and cost efficiency in broad portfolios of securities. ETFs trade on the exchange; can be bought or sold at any point during market hours; can be shorted or purchased on margin; and risk can be managed with techniques such as stop loss and limit orders.

As the popularity of ETFs has grown, so too has the number of product offerings and there is a wide array. Some track indices or sectors while others represent more specialized areas of the market. Making choices is dependent on the goals investors wish to achieve.

For example, many investors wanting exposure to popular IPOs that were otherwise difficult to access, such as LinkedIn, purchased the Global Social Media Index (NASDAQ: SOCL). It's a specialty ETF that seeks to provide investment results aligned with the Solactive Social Media Index. Others use ETFs to address more specific goals.

Is the price of beef and pork going to rise with cattle and hog producers being buffeted by rising feed costs? The iPath Dow Jones-USB Livestock Subindex Total Return (NYSE: COW) provides access to live cattle and lean hogs. Is potable water going to be an increasingly rare commodity? The Guggenheim S&P Global Water Index (NYSE: CGW) is comprised of about 50 companies from different segments in the water industry. Will lithium batteries be the final answer for low-emission automobiles? The Global X Lithium ETF (NYSE: LIT) holds the largest and most liquid companies listed in the lithium space.

Some investors are replacing mutual fund holdings with ETFs, a trend not lost on the mutual fund industry. The ETF community was abuzz when PIMCO's founder Bill Gross brought out an ETF closely resembling his flagship mutual fund. The PIMCO Total Return ETF (NYSE: BOND) has the same goals as the mutual fund, but without the same derivatives exposure. Many mutual fund investors switched to the ETF, looking for similar returns at a lower cost.

Leveraged and inverse-leveraged ETFs are an area of interest for some investors. These ETFs are designed to provide a return that is a multiple of an underlying benchmark on a daily basis, by betting on market movements. A popular one in Canada is the Horizon BetaPro Global Gold Bull+ & Bear+ ETF (TSX: HGU/HGD), which seeks daily investment results equal to 200% the daily

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performance, or inverse performance, of the S&P/TSX Global Gold Index.

However, due to the mathematics of compounding and rebalancing, holding leveraged or inverse-leveraged ETFs longer than a single trading day can be risky. Investors should use extreme caution.

While this makes for a much more interesting investing landscape, it can also be overwhelming. As with any investment decision, care must be taken to understand the intricacies. Just because there are fancy ETFs on the market, does not mean they are suitable for every portfolio. Remember: "If you don't understand it, don't buy it."

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