

# National Bank Direct Brokerage



Invest the market newsletter - May 2013 - Volume VI, number 5












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 <b>BOMBARDIER</b> <b>BBD.B</b> <hr style="width: 100%;"/>	 <b>Bank of America</b>  <b>BAC</b> <hr style="width: 100%;"/>
 <b>ORBITE</b> <b>ORT</b> <hr style="width: 100%;"/>	 <b>FB</b> <hr style="width: 100%;"/>
 <b>NA</b> <hr style="width: 100%;"/>	 <b>C</b> <hr style="width: 100%;"/>
 <b>SUNCOR</b> <b>ENERGY</b> <b>SU</b> <hr style="width: 100%;"/>	 <b>GE</b> <hr style="width: 100%;"/>

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## INTRODUCING OUR ETF CENTRE!

Dear Ugo-2 Tessier,

## Large Cap Canadian Equity ETF

Special collaboration: Ian Gascon

Nearly everywhere in the world, investors have a bias that incites them to invest a significant portion of their portfolio in the local market, in their own country. This bias can be explained in part by the perception of having a better knowledge of one's own market, by a lower transaction cost or by higher tax efficiency. Canada is no exception to this observation and Canadian shares likely make up a significant proportion of your portfolio.

There are more than 50 ETFs in Canada that invest primarily in Canadian shares, some very diversified, some sectoral, some with distinctive approaches (fundamental indexation, covered calls, securities, low-volatility stocks...). The objective of this article is not to start a debate on the merit of these approaches, but to analyze the exposure of the ETF stocks that are most representative of the Canadian market. Only 5 ETFs meet these criteria and attempt to replicate large cap passive indexes. These are only 5 ETFs among more than 265 (less than 2%) offered in Canada, but they represent more than 25% of all ETF assets under management in Canada. To help you make a more informed choice, here are the main differences between these ETFs.

The most well known, most liquid, the one with the most assets under management (\$11B) and the oldest one is the iShares S&P/TSX 60 Index Fund (XIU) that follows the S&P/TSX 60 index. As its name indicates, this fund invests in 60 large cap Canadian equities. The 10 largest securities represent more than 45% of this ETF, which makes it an ETF that is very concentrated in only a few securities. The financial, energy and materials sectors, which are representative of the Canadian market, dominate this ETF. However, with a management expense ratio (MER) of 0.18%, it is not the least expensive. For active investors or those who are looking for temporary exposure to the Canadian equity market, this may be the right choice.

A direct competitor of the XIU is the Horizons S&P/TSX 60 Index ETF (HXT). It follows the same index, but is structured differently. Using term contracts, the HXT does not invest directly in underlying securities. This particular structure allows it to replicate the S&P/TSX 60 index (overall return) with a potential tracking error that is lower than the XIU and without necessarily distributing to shareholders, which may have tax advantages for certain investors. Normally, this type of structure using term contracts has higher fees (like its American counterpart, the Horizons S&P 500 Index ETF (HXS), or in the case of the iShares Advantaged line) that vary between 0.30% and 0.75% per year, but since its launch, the HXT is taking advantage of an agreement in which no fees are charged for the derivative. However, this advantage must be analyzed to take into account the counterparty risk from using a derivative and the possibility that this particular agreement does not get renewed. It

should be noted that following the changes announced during the last federal budget, Horizons, this ETF's manager, does not expect this HXT to be affected by the new tax rules concerning the "qualification operations". In short, with fees of 0.07% (currently reduced to 0.05% until October 2013) and an MER of 0.08%, this ETF is the least expensive in Canada and offers the possibility for exposure to Canadian equities with tax advantages, which is a point to be considered for non-tax sheltered accounts.



The iShares S&P/TSX Capped Composite Index Fund (XIC) attempts to replicate the S&P/TSX Capped Composite index, an index that is larger than the S&P/TSX 60, with more than 200 securities. The sector exposure is similar but more diversified. The 10 largest securities represent less than 35% of this ETF, which should be a long-term advantage compared to the more concentrated S&P/TSX 60 index. With an MER of 0.27%, this ETF is relatively expensive for the kind of exposure it offers. The BMO S&P/TSX Capped Composite Index ETF (ZCN) also follows the S&P/TSX Capped Composite index, but its fees are 0.10% less than the XIC (with an MER of 0.17%), which potentially makes it a better choice than the XIC. In both cases, the liquidity offered on the secondary market is excellent and both funds have tracking errors that are coherent with their management fees.

**Contact us**

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Halfway between the S&P/TSX 60 index and the S&P/TSX Capped Composite index, from a diversification point of view, is the index that is followed by the Vanguard FTSE Canada Index ETF (VCE), an ETF with an MER of 0.11%, which makes it the least expensive in Canada after the HXT (see above). With approximately \$140M in assets, it is currently the smallest of the other comparable ETFs. The VCE now follows the FTSE Canada index that is composed of approximately 80 securities and whose sector exposure is, once again, similar to the other indexes. In my opinion, this ETF was more interesting before the recent index change. Now that it follows a less diversified index with a less expensive license fees, Vanguard appears to be banking on its favourable MER to grow the VCE's assets.

**About Ian Gascon**

Ian Gascon is president of Idema Investments ([www.idema.ca](http://www.idema.ca)), a portfolio manager specialized in exchange traded funds that offers personalized portfolios for independent investors, among other services. He is the author of an ETF blog on [lesaffaires.com](http://lesaffaires.com).

Mr. Gascon holds a Masters in Finance from HEC Montreal (M.Sc.), as well as a Graduate Diploma in Management (DESG) and a bachelor's degree in engineering, aeronautics major, (B.Eng.) from Polytechnique Montréal. He is registered with the AMF as a Portfolio Manager, Designated Person and Chief Compliance Officer.

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**Upcoming seminars**

Subject (Language of the event)	Date	Place
<a href="#">Tools for self-directed investors</a> (French)	Tuesday May 7, 2013 Time: 7 P.M. to 9 P.M.	Quebec
	Wednesday May 22, 2013 Time: 7 P.M. to 9 P.M.	La Prairie
<a href="#">Getting started with ETFs</a> (English)	Tuesday May 7, 2013 Time: 6:30 P.M. to 8:30 P.M.	Richmond
<a href="#">Recognia, An Interactive Technical Analysis Tool</a> (French) <a href="#">Recognia, An Interactive Technical Analysis Tool</a> (English)	Wednesday May 8, 2013 Time: 12 P.M. to 1 P.M.	Online
	Wednesday May 8, 2013 Time: 7 P.M. to 8 P.M.	Online
<a href="#">Generating Income using ETFs</a> (English)	Wednesday May 8, 2013 Time: 12 P.M. to 1 P.M.	Vancouver
<a href="#">Using ETFs for your Equity Portfolio</a>	Tuesday May 14, 2013	Toronto

(English)	Time: 12 P.M. to 1 P.M.	Montreal
<a href="#">Introduction to ETFs in the context of portfolio building</a> (French)	Wednesday May 15, 2013 Time: 7 P.M. to 9 P.M.	Montreal
	Wednesday May 29, 2013 Time: 7 P.M. to 9 P.M.	Quebec
<a href="#">Building a Better Portfolio Using ETFs</a> (French)	Tuesday May 28, 2013 Time: 7 P.M. to 9 P.M.	Montreal

## New Issues

### Diversified GICs

**Canadian Advantage 8 GIC (5 years)**

**Canadian Advantage 8 GIC (3.5 years)**

**Issue Date:** May 24, 2013

**Sales Period:** April 15, 2013 to May 17, 2013

**Maturity Date:**

- Diversified GICs: May 23, 2018
- Canadian Advantage 8 GIC (5 years): May 23, 2018
- Canadian Advantage 8 GIC (3.5 years): November 23, 2016

### Terms and conditions:

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### Information:

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