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ETF INVESTING

Latin, energy ETFs shine in quarter

New dividend, microcap funds debut; firm files active ETF

By [John Spence](#), MarketWatchLast Update: 12:05 AM ET Sept. 30, 2005 [[Page 1](#) | [2](#)][E-mail it](#) | [Print](#) | [Discuss](#) | [Alert](#) | [Reprint](#) | [RSS](#)**BOSTON (MarketWatch) --** A glance at the best-performing exchange-traded funds in the third quarter underscores how much energy has dominated investors' mindsets.

Over the past three months, ETFs focused on Latin American and energy stocks have been the best place to be, as they have been for some time now.

Meanwhile, ETF providers trotted out new dividend, international and U.S. microcap offerings, and elusive actively managed funds took another step forward, although observers don't expect them to debut anytime soon.

The top ETFs in the quarter through Sept. 28 were iShares MSCI Brazil ([EWZ](#): [news](#), [chart](#), [profile](#)), with a 34.8% gain, and iShares S&P Latin America 40 ([ILF](#): [news](#), [chart](#), [profile](#)), which added 27.5%.

Highlighting the weakness of the dollar and a Latin American economic boom driven largely by energy, the Brazilian ETF is up 86.1% over the past 12 months, while the broader regional fund has added 80.7%, according to financial-research firm Morningstar Inc. At the same time, the iShares MSCI Mexico ([EWW](#): [news](#), [chart](#), [profile](#)) surged 18.6% in the quarter and 58.7% over the past year.

Yet despite those high-flying returns, emerging markets -- and Latin American funds in particular -- are risky and prone to wide swings in performance. For example, Morningstar notes that over

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the past decade, Latin American funds have suffered double-digit losses over three months 21 times, shedding at least 20% in nine of those quarters.

Not surprisingly, energy and natural resources funds also topped the performance charts on surging oil prices. Vanguard Energy Vipers ([VDE: news, chart, profile](#)), Energy Select Sector SPDR ([XLE: news, chart, profile](#)), iShares Goldman Sachs Natural Resources ([IGE: news, chart, profile](#)) and iShares Dow Jones U.S. Energy ([IYE: news, chart, profile](#)) all gained at least 15% for the quarter.

Meanwhile, a new ETF focused on renewable-energy companies, PowerShares WilderHill Clean Energy ([PBW: news, chart, profile](#)), posted a 15% gain. The fund has seen an upswing in assets and investor interest after Hurricanes Katrina and Rita disrupted oil facilities in the Gulf Coast.

"Skyrocketing oil prices are making alternative energy sources and investments more compelling and attractive," said Andrew Brengle, senior research analyst at socially responsible investing firm KLD Research & Analytics Inc.

Among U.S. ETFs, stocks outperformed bonds in the third quarter as the S&P 500-tracking SPDR 500 Trust ([SPY: news, chart, profile](#)) added 1.7%; the iShares Lehman Aggregate Bond ([AGG: news, chart, profile](#)) lost 0.4%, according to Morningstar. The iShares MSCI EAFE ([EFA: news, chart, profile](#)), which tracks a broad yardstick for international stocks, outpaced both funds with a 9.7% gain as the dollar slid relative to foreign currencies and investors favored foreign equities.

Real estate ETFs also posted another positive quarter as the StreetTracks Wilshire REIT ([RWR: news, chart, profile](#)) gained 4.1%.

ETF expansion rolls on

Although it seems ETF managers have snapped up every index under the sun, the \$252 billion industry continued to grow in the quarter with new funds tracking microcaps, dividend-payers and international "style" benchmarks.

Seeking to capitalize on the popularity of income-producing stocks, PowerShares Capital Management expanded its lineup with a trio of new dividend ETFs, including one focused on international stocks, PowerShares International Dividend Achievers Portfolio ([PID: news, chart, profile](#)).

Vanguard also unveiled plans to introduce an index fund and matching ETF share class hitched to an index rich in dividend-paying companies, maintained by financial-data provider Mergent Inc. Finally, State Street Global Advisors says it is readying its own ETF based on a new benchmark

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from Standard & Poor's.

Barclays Global Investors, the 800-pound gorilla of the industry, broadened its offerings as well with the first ETFs that break up foreign stocks along growth and value lines: iShares MSCI EAFE Growth ([EFG: news, chart, profile](#)) and iShares MSCI EAFE Value ([EFV: news, chart, profile](#)) .

Investors witnessed the launch of the first ETFs focused on microcap ETFs: PowerShares Zacks Micro Cap Portfolio ([PZI: news, chart, profile](#)) and iShares Russell Microcap Index ([IWC: news, chart, profile](#)) .

A third microcap fund, First Trust Dow Jones Select MicroCap Index, was slated to begin trading on Friday on the American Stock Exchange, signaling the entry of a new firm into the ETF fray.

What's on tap

Active ETFs took another step forward when a start-up firm co-founded by one of the foremost experts in exchange-traded funds recently filed documents with the Securities and Exchange Commission that would create the first such instrument.

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John Spence is a reporter for MarketWatch in Boston.

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However, industry observers aren't holding their breath to see these products anytime soon, given what they describe as the complexity of the structure and an overstretched SEC.

Managed ETFs LLC, a New Jersey-based company, has proposed a format that seeks to get around the disclosure issues that have hampered the creation of active ETFs. Co-founder Gary Gastineau, a former executive at the American Stock Exchange and Nuveen Investments, is known as an ETF whiz in industry circles.

Thus far, ETFs have tracked indexes of stocks or bonds, without a manager actively picking securities in an effort to beat the market. Yet with ETFs ballooning and more growth predicted, actively managed versions of the financial instruments are seen as a Holy Grail of sorts.

In the filing, Gastineau's firm has proposed a structure where ETF holdings would be disclosed on a limited basis, a structure that might not fly with regulators due to a lack of transparency.

In other areas, ETF providers and exchanges are said to be developing more broad-based commodities funds after the launch of the first gold ETFs.

BGI currently has a silver ETF in registration, and oil funds are seen coming down the pike. However, it might not be practical for an oil fund to hold the physical commodity like the gold funds, so derivatives are seen as a possible solution, although such a structure has not been approved by the SEC.

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Top-performing ETFs in third quarter

Name (Ticker)	Q3 (%)	1 yr (%)	3 yr (%)
iShares MSCI Brazil (Free) Index EWZ	34.8	86.2	82.2
iShares S&P Latin America 40 Index ILF	27.5	80.7	57.1
iShares MSCI South Africa Index EZA	23.5	39.9	---
iShares MSCI South Korea Index EWY	22.1	59.3	29.9
Vanguard Energy Vipers VDE	21.2	55.2	---

Worst-performing ETFs in third quarter

Name (Ticker)	Q3 (%)	1 yr (%)	3 yr (%)
Consumer Discretionary SPDR XLY	-3.45	4.01	11.53
iShares Dow Jones US Consumer Services IYC	-3.63	6.87	10.65
Vanguard Consumer Discretionary VIPERs VCR	-3.83	8.11	---
PowerShares Dyn Leisure & Entertainment PEJ	-6.16	---	---
iShares MSCI Taiwan Index EWT	-9.89	5.69	15.4

Source: Morningstar Inc., (as of 9/28/05)

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