# How To Avoid the Worst Style ETFs

Question: Why are there so many ETFs?

Answer: ETF providers tend to make lots of money on each ETF so they create more products to sell.

The large number of ETFs has little to do with serving your best interests. Below are three red flags you can use to avoid the worst ETFs:

**1. Inadequate Liquidity**

This issue is the easiest to avoid, and our advice is simple. Avoid all ETFs with less than $100 million in assets. Low levels of liquidity can lead to a discrepancy between the price of the ETF and the underlying value of the securities it holds. Plus, low asset levels tend to mean lower volume in the ETF and larger bid-ask spreads.

**2. High Fees**

ETFs should be cheap, but not all of them are. The first step here is to know what is cheap and expensive.

To ensure you are paying at or below average fees, invest only in ETFs with total annual costs below 0.49%, which is the average total annual cost of the 289 U.S. equity Style ETFs we cover.

Figure 1 shows the most and least expensive Style ETFs. QuantShares provides three of the most expensive ETFs while Schwab ETFs are among the cheapest.

**Figure 1: 5 Least and Most-Expensive Style ETFs**

| Ticker | Name | Style | Total Annual Cost |
|---|---|---|---|
| | **Most Expensive** | | |
| MOM | QuantShares U.S. Market Neutral Momentum | Mid Cap Growth | 1.66% |
| CHEP | QuantShares U.S. Market Neutral Value | Mid Cap Value | 1.66% |
| SIZ | QuantShares U.S. Market Neutral Size | Small Cap Blend | 1.66% |
| FWDD | AdvisorShares Madrona Forward Domestic | All Cap Blend | 1.39% |
| WBIG | WBI Large Cap Tactical Yield Shares | All Cap Blend | 1.11% |
| | **Least Expensive** | | |
| SCHX | Schwab U.S. Large-Cap | Large Cap Blend | 0.04% |
| SCHB | Schwab U.S. Broad Market | All Cap Blend | 0.04% |
| VOO | Vanguard S&P 500 | Large Cap Blend | 0.06% |
| VTI | Vanguard Total Stock Market | All Cap Blend | 0.06% |
| IVV | iShares Core S&P 500 Index | Large Cap Blend | 0.08% |

Sources: New Constructs, LLC and company filings

Investors need not pay high fees for quality holdings. Arrow QVM Equity Factor (QVM) earns our Very Attractive rating and has low total annual costs of only 0.72%.

On the other hand, no matter how cheap an ETF, if it holds bad stocks, its performance will be bad. The quality of an ETFs holdings matters more than its price.

**3. Poor Holdings**

Avoiding poor holdings is by far the hardest part of avoiding bad ETFs, but it is also the most important because an ETF's performance is determined more by its holdings than its costs. Figure 2 shows the ETFs within each style with the worst holdings or portfolio management ratings.

**Figure 2: Style ETFs with the Worst Holdings**

| Ticker | Name | Style | Portfolio Management Rating |
|---|---|---|---|
| PRFZ | PowerShares FTSE RAFI US 15000 Small-Mid | All Cap Blend | Dangerous |
| ARKK | Ark Innovation ETF | Large Cap Blend | Dangerous |
| RWG | Columbia RP Focused Large Cap Growth | Large Cap Growth | Dangerous |
| SYV | State Street SPDR MFS Systematic Value Equity | Large Cap Value | Dangerous |
| RSCO | State Street SPDR Russell Small Cap Completeness | Mid Cap Blend | Dangerous |
| ARKQ | Ark Industrial Innovation ETF | Mid Cap Growth | Dangerous |
| RWK | RevenueShares Mid Cap Fund | Mid Cap Value | Dangerous |
| IWC | iShares Russell Microcap | Small Cap Blend | Dangerous |
| IWO | iShares Russell 2000 Growth | Small Cap Growth | Dangerous |
| PXSV | PowerShares Russell 2000 Pure Value | Small Cap Value | Dangerous |

Sources: New Constructs, LLC and company filings

State Street, iShares, and PowerShares appear more often than any other providers in Figure 2, which means that they offer the most ETFs with the worst holdings.

Our overall ratings on ETFs are based primarily on our stock ratings of their holdings.

**The Danger Within**

Buying an ETF without analyzing its holdings is like buying a stock without analyzing its business and finances. Put another way, research on ETF holdings is necessary due diligence because an ETF's performance is only as good as its holdings' performance.

PERFORMANCE OF ETF's HOLDINGS = PERFORMANCE OF ETF

*Disclosure: David Trainer and Max Lee receive no compensation to write about any specific stock, style, or theme.*

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2. Standard for all companies.
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