



How to Avoid the Worst Style ETFs

Question: Why are there so many ETFs?

Answer: ETF issuance is profitable, so Wall Street keeps cranking out more products to sell.

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The large number of ETFs has little to do with serving your best interests as an investor. More [reliable](#) & [proprietary](#) fundamental data, proven in [The Journal of Financial Economics](#), drives our research and analysis of ETF holdings and provides investors with a [new source of alpha](#). We leverage this data to identify 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. Small ETFs also generally have lower trading volume, which translates to higher trading costs via larger bid-ask spreads.

2. High Fees

ETFs should be cheap, but not all of them are. The first step is to benchmark what cheap means.

To ensure you are paying at or below average fees, invest only in ETFs with [total annual costs](#) below 0.48%, – the average total annual cost of the 897 U.S. equity Style ETFs we cover. The weighted average is lower at 0.13%, which highlights how investors tend to put their [money in ETFs with low fees](#).

Figure 1 shows Infrastructure Capital Equity Income ETF (ICAP) is the most expensive style ETF and State Street SPDR Portfolio S&P 500 ETF (SPLG) is the least expensive. WBI provides three of the most expensive ETFs while State Street ETFs are among the cheapest.

Figure 1: 5 Most and Least Expensive Style ETFs

Ticker	Name	Style	Total Annual Cost
Most Expensive			
ICAP	Infrastructure Capital Equity Income ETF	All Cap Value	3.62%
SCAP	Infrastructure Capital Small Cap Income ETF	Small Cap Blend	2.20%
WBIF	WBI BullBear Value 3000 ETF	All Cap Blend	1.70%
WBIG	WBI BullBear Yield 3000 ETF	All Cap Blend	1.66%
WBIL	WBI BullBear Quality 3000 ETF	All Cap Blend	1.62%
Least Expensive			
SPLG	State Street SPDR Portfolio S&P 500 ETF	Large Cap Blend	0.02%
BBUS	JPMorgan BetaBuilders U.S. Equity ETF	Large Cap Blend	0.02%
IVV	iShares Core S&P 500 ETF	Large Cap Blend	0.03%
SPTM	State Street SPDR Portfolio S&P 1500 Composite Stock Market	Large Cap Blend	0.03%
VOO	Vanguard 500 Index Fund	Large Cap Blend	0.03%

Sources: New Constructs, LLC and company filings



Investors need not pay high fees for quality holdings.¹ iShares Core S&P 500 ETF (IVV) is the best ranked style ETF in Figure 1. IVV's Neutral [Portfolio Management rating](#) and 0.03% total annual cost earns it an Attractive rating.² Alpha Architect U.S. Quantitative Value ETF (QVAL) is one of the best ranked style ETFs overall. QVAL's Attractive Portfolio Management rating and 0.32% total annual cost earns it a Very Attractive rating.

On the other hand, Vanguard Small Cap Index Fund (VB) holds poor stocks and earns our Unattractive rating, despite having low total annual costs of 0.06%. No matter how cheap an ETF looks, if it holds bad stocks, its performance will be bad. The quality of an ETF's holdings matters more than its management fee.

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 [portfolio management ratings](#), a function of the fund's holdings.

Figure 2: Style ETFs with the Worst Holdings

Ticker	Name	Style	Portfolio Management Rating
SRHR	SRH REIT Covered Call ETF	All Cap Blend	Unattractive
IPO	Renaissance IPO ETF	All Cap Growth	Unattractive
XSHD	Invesco S&P Small Cap High Dividend Low Volatility	All Cap Value	Unattractive
SFY	Tidal Trust SoFi Select 500 ETF	Large Cap Blend	Unattractive
SPYG	State Street SPDR Portfolio S&P 500 Growth ETF	Large Cap Growth	Unattractive
FFLV	Fidelity Fundamental Large Cap Value ETF	Large Cap Value	Unattractive
PJFM	PGIM Jennison Focused Mid Cap ETF	Mid Cap Blend	Unattractive
AWEG	Alger Weatherbie Enduring Growth ETF	Mid Cap Growth	Unattractive
IMCV	iShares Morningstar Mid Cap Value ETF	Mid Cap Value	Unattractive
QQQS	Invesco NASDAQ Future Gen 200 ETF	Small Cap Blend	Unattractive
TMFS	Motley Fool Small Cap Growth ETF	Small Cap Growth	Unattractive
RZV	Invesco S&P Small Cap 600 Pure Value ETF	Small Cap Value	Unattractive

Sources: New Constructs, LLC and company filings

Invesco appears more often than any other providers in Figure 2, which means that they offer the most ETFs with the worst holdings.

Invesco NASDAQ Future Gen 200 ETF (QQQS) is the worst rated ETF in Figure 2 based on our [predictive overall rating](#). Motley Fool Small Cap Growth ETF (TMFS), Renaissance IPO ETF (IPO), and Invesco S&P Small Cap 600 Pure Value ETF (RZV) also earn a Very Unattractive predictive overall rating, which means not only do they hold poor stocks, they charge high total annual costs.

Our [overall ratings on ETFs](#) are on our [stock ratings](#) of their holdings and the total annual costs of investing in the ETF.

The Danger Within

Buying an ETF without analyzing its holdings is like buying a stock without analyzing its business model 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. Don't just take our word for it, [see what Barron's says](#) on this matter.

PERFORMANCE OF ETFs HOLDINGS – FEES = PERFORMANCE OF ETF

¹ Three independent studies from respected institutions prove the superiority of our data, models, and ratings. Learn more [here](#).

² Harvard Business School features the powerful impact of our research automation technology in the case [New Constructs: Disrupting Fundamental Analysis with Robo-Analysts](#).



Analyzing each holding within funds is no small task. Our [Robo-Analyst technology](#) enables us to perform this diligence with scale and provide the [research needed](#) to [fulfill the fiduciary duty of care](#). More of the biggest names in the financial industry (see [At BlackRock, Machines Are Rising Over Managers to Pick Stocks](#)) are now embracing technology to leverage machines in the investment research process. Technology may be the only solution to the dual mandate for research: cut costs and fulfill the fiduciary duty of care. Investors, clients, advisors and analysts deserve the latest technology to get the diligence required to make prudent investment decisions.

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Many firms claim their research is superior, but none of them can prove it with independent studies from highly-respected institutions as we can. Three different papers from both the public and private sectors show:

1. The stock market is missing footnotes – and only we have that critical data.
2. Legacy fundamental datasets suffer from significant inaccuracies, omissions, and biases.
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Best Fundamental Data in the World

In [The Journal of Financial Economics](#), a top peer-reviewed journal, [Core Earnings: New Data & Evidence](#) proves our Robo-Analyst technology overcomes material shortcomings in legacy firms' data collection processes to provide superior [fundamental data](#), [earnings](#) models, and [research](#). More [details](#).

Key quotes from the paper:

- “[New Constructs’] *Total Adjustments* differs significantly from the items identified and excluded from Compustat’s adjusted earnings measures. For example... 50% to 70% of the variation in *Total Adjustments* is not explained by S&P Global’s (*SPGI*) *Adjustments* individually.” – pp. 14, 1st para.
- “A final source of differences [between New Constructs’ and S&P Global’s data] is due to data collection oversights...we identified cases where Compustat did not collect information relating to firms’ income that is useful in assessing core earnings.” – pp. 16, 2nd para.

Superior Models

Ernst & Young features the superiority of our ROIC, NOPAT and Invested Capital research to Capital IQ & Bloomberg’s in [Getting ROIC Right](#). See the [Appendix](#) for direct comparison details.

Key quotes from the paper:

- “...an accurate calculation of ROIC requires more diligence than often occurs in some of the common, off-the-shelf ROIC calculations. Only by scouring the footnotes and the MD&A [as New Constructs does] can investors get an accurate calculation of ROIC.” – pp. 8, 5th para.
- “The majority of the difference...comes from New Constructs’ machine learning approach, which leverages technology to calculate ROIC by applying accounting adjustments that may be buried deeply in the footnotes across thousands of companies.” – pp. 4, 2nd para.

Superior Stock Ratings

Robo-Analysts’ stock ratings outperform those from human analysts as shown in this [paper](#) from Harvard Business School. Bloomberg features the paper [here](#).

Key quotes from the paper:

- “the portfolios formed following the buy recommendations of Robo-Analysts earn abnormal returns that are statistically and economically significant.” – pp. 6, 3rd para.
- “Our results ultimately suggest that Robo-Analysts are a valuable, alternative information intermediary to traditional sell-side analysts.” – pp. 20, 3rd para.

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