Title:
Eight Rules For ETF Success

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Summary:
Managing a global portfolio of exchange-traded funds (ETFs) is a great way to build a diversified portfolio with exposure to equities around the globe. Fortunately, you need not be a rocket scientist to do this, but many investors fail to observe some basic guidelines, and it can get them into real trouble. Follow these eight steps and sleep easier.

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Article Body:
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1. Liquidity Comes First: Before you even think of building an investment portfolio, you should set aside about six months of income in a “rainy day” account. This could be put into a money market fund or U.S. Treasury securities. Having this money set aside will ease your mind and allow you to be more open and creative with your global portfolios.

2. Separate Portfolios: You should separate your core conservative portfolio from your growth portfolios. With the core conservative portfolio, your top priority is capital preservation, and growth is a secondary consideration. Your growth portfolios are more speculative, with capital growth as the primary goal.

3. Really Diversify Your Portfolios: You need positions in your portfolios that are likely to offset each other as unexpected events and market movements become a reality. This is not accomplished with different sectors of ETFs or a mix of small-cap, mid-cap and large-cap ETFs. Rather the goal is to have some

investments that are on both sides of risks.

For example, if the U.S. dollar declines, have some investments in precious metals or denominated in other currencies, such as Switzerland or Australia or Singapore ETFs. If inflation heats up, have some investments that hedge this risk such as timber, gold or Treasury inflation-protected bonds (TIPs). If political events or policies in one country take a turn for the worst, it is helpful to have investments in other well-developed countries to offset any loss of value. You get the idea, spread your risk and avoid having one ETF account for more than 5%-10% of your core portfolio.

4. Be Careful Which Countries You Pick: You need some guidelines to help keep you from getting carried away and having too concentrated a position in a particular country or region. In particular, take a good look at the following: 1) the stability and overall political and corporate governance; 2) the legal environment, respect for contracts, low levels of corruption, due process and rule of law; 3) the macroeconomic environment including fiscal discipline and currency strength; and 4) political risks that could affect financial markets.

Keep in mind that the quality of the countries you choose to invest in is the primary but not the only factor. The price or valuation of a country’s stock market is also extremely important. Oftentimes, the best time to buy into a country’s stock market is when it is beaten down, but there are signs that its economic and political problems will sharply improve. If you have a long-term perspective, you might consider annuities specially structured for ETF portfolios.

5. Minimize Company Risk by using our “buy countries, not stocks” strategy. Instead of trying to pick the best three stocks on the Tokyo Stock Exchange, why not just minimize company risk by buying the iShares MSCI Japan Index, which tracks the Nikkei 225 and spreads this risk across 225 Japanese companies.

6. Monitor ETF Country And Company Exposure: Be careful to look under the hood of ETFs to see where your money is going. For example, let’s look at the iShares MSCI Emerging Markets ETF. It invests in 26 different countries, so it is natural to think that you will get broad exposure to all 26 countries. You would be wrong: 50% of your investment in this fund is going to four countries: South Korea, South Africa, Taiwan and China. In addition, incredibly, 7.5% is going to one company, Samsung Electronics of South Korea.

The same is true for the MSCI Europe, Asia and Far East index. It contains 21 developed countries, but 48% of the money you invest would go to just two: Japan and the United Kingdom. Meanwhile, less than 1% would go to Singapore and

Ireland! Country specific ETFs such as the new iShares FTSE/Xinhua China 25 Index can also have a fair amount of concentrated risk. Although the China ETF tracks a basket of 25 companies, the largest five companies account for nearly 50% of your exposure.

7. Cut Losses With A Trailing Stop-Loss Policy And ETF Put Options: We have all been there. You buy a stock or fund, and it appreciates in value rapidly. Then it stumbles and begins to decline. What do you do? Should you buy more, let it ride, or sell? Save yourself a lot of pain and agony by following a simple rule. If a position ever falls more than 20% from its high, sell it immediately and reassess the situation. If you invest in an ETF with a sizable downside risk, why not spend a few hundred dollars to purchase a put-option as an insurance policy?

8. Rebalance Your Portfolio: At least annually, you need to make some changes so that you are not overly exposed to countries that have higher risk factors and volatility. One way is by selling some shares of your winners and increasing exposure to under performers. This accomplishes another goal, locking in gains and taking some money off the table. Remember, only a fool holds out for top dollar, especially in the more volatile emerging market countries.

Building your portfolios with low-cost, tax-efficient ETFs is a smart strategy, but don’t set it on auto pilot.

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