Understanding
Exchange Traded Funds (ETFs)

Exchange traded funds (ETFs) are an open-ended investment fund, similar to a traditional managed fund, which is traded on the ASX, and are a low-cost way to earn a return similar to an index or a commodity. They can also help to diversify your investments. You can buy and sell units in ETFs through a stockbroker on the Australian Securities Exchange, the same way you buy and sell shares.

In Australia, most ETFs don't try to outperform the market. The role of the fund manager is to track the value of:

- an index, for example the ASX200 or S&P500; or
- a specific commodity, such as gold.
- The value of the ETF will be determined by the ups and downs of the index or asset they're tracking.

What you can Invest in through an ETF

ETFs are available for a range of asset classes and individual assets.
These include:

- Australian shares;
- international shares;
- sectors of the Australian or international share market, such as mining or financials;
- fixed income investments like bonds;
- precious metals and commodities;
- foreign currencies;
- crypto assets.

Advantages of ETFs

- **Simplicity and Diversification** – ETFs help investors gain exposure to a range of investment strategies, geographic regions, and asset classes in a single trade. This can help with diversification and allows you to invest in markets or assets it can be difficult or expensive to access.
- **Transparency –** Information relating to ETFs, including underlying portfolio holdings and fees, can be accessed at any time via the fund manager's website.
- **Low cost** – a lot of ETFs have a low management expense ratio (MER) and do not have in-built 'active management' fees seen in some managed funds.
- **Liquidity and Easy to trade** – you can buy and sell ETFs during the trading hours of the exchange.
- **SMSF Friendly** – ETFs are eligible to be bought inside Self-Managed Super Funds just like shares.

Things you should know

- The balance and return of your investment are not guaranteed – the value of your investment will rise and fall with market movements;
- Income and capital gains distributed from your ETF are added to your assessable income each year and will need to be included in your annual Tax Return, even if you have opted to reinvest all income back in the ETF. These details are included in the Annual Taxation Statement of the managed fund each year. As this is added to your assessable income, it may affect your other benefits such as Centrelink benefits, Family Tax Benefits and Child Support (where applicable);
- When you redeem your funds or sell out of an ETF, you may pay Capital Gains Tax on any profit (or gain) made.
- Some products track an index or asset and 'look' like an ETF. But they're not ETFs and they can be riskier. These products include:
  - exchange traded commodities
  - exchange traded notes
  - exchange traded certificates
  - exchange traded securities
- There are also exchange traded managed funds and exchange traded hedge funds. With these, the investment manager tries to outperform an index and may use high risk trading strategies.
- If the ETF invests in international assets, you face the risk of currency movements impacting your returns.
- Some ETFs invest in assets that are not liquid, such as emerging market debt. This can make it difficult at times for the ETF provider to create or redeem securities.

Source: https://moneysmart.gov.au/managed-funds-and-etfs/exchange-traded-funds-etfs