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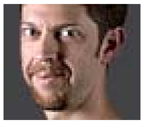

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PERSONAL FINANCE

ETFs for everyone. Even dermatology investors

Infectious diseases, anyone? What about cancer, or metabolic endocrine disorders? Or, how about ophthalmology -- can you see an investing potential in that?

The exchange-traded fund industry can, and that's why there are new ETFs that allow you to invest in health care stocks specializing in each of these areas. These new funds may sound gimmicky, but they're representative of what's new and hot for spring in the ETF business.

The ETF business today is a circus. Close to 100 new ones have been listed for trading on North American exchanges so far this year, compared with 170 in all of last year and about 60 in 2005. It's quite a change from the early days of ETFs a decade ago, when there was only an obscure handful of these index funds that trade like a stock.

ETFs began by tracking major global stock indexes such as the S&P 500, the Nasdaq 100 and the S&P/TSX composite (and its predecessor, the TSE 300 index). Today, with a choice of funds for virtually all major indexes, ETF providers are turning to more exotic products to build their franchises.

So far this year, a firm called XShares Advisors has launched 16 ETFs in its HealthShares series, including the aforementioned funds as well as others in areas such as cardiology and neuroscience. Digging deep into a particular sector, health care in this case, is one apparent theme in new ETF products. Here are some others.

>>Niche products for mainstream investors: Preferred-share ETFs have been issued recently in both the Canadian and U.S. markets, while a high-yield bond ETF and other funds that cover global infrastructure companies have just been listed on U.S. exchanges.

>>Products for exploiting down markets: These funds allow investors to profit from declining stock markets and commodity prices; big players include ProShares in the U.S. market and BetaPro in Canada.

>>Oddball ideas: An example would be the Claymore/Ocean Tomo Growth Index ETF, a new spin on an existing product (the Claymore/Ocean Tomo Patent ETF) that focuses on companies with the most valuable patents.

There's a growing sense that ETF providers are getting carried away with some of the new products they're introducing. "They're using a 'throw it against the wall and see what sticks approach,' "said Tyler Mordy, head of research at Hahn Investment Stewards and editor of a publication called ETFocus. "It's getting ridiculous."

Russel Kinnel, direct of mutual fund research at the independent U.S. analysis firm Morningstar, was especially caustic in an online commentary about new ETFs earlier this month. Mr. Kinnel said most long-term investors will do fine in ETFs, but he also used the phrase "speculative dross" in assessing some new products and warned about a "casino side of the ETF world."

If you're an investor trying to make sense of the ever-expanding ETF universe, here's some help. There are really only three categories of ETFs -- funds you need because they're core products, discretionary funds that you might like to have, and everything else.

The essential funds are the ones covering the broad-based indexes that investors need to build a diversified portfolio. Included in this group are ETFs covering the Canadian, U.S. and global markets, as well as emerging markets and the bond market here in Canada.

Discretionary funds include well-established sector ETFs in areas such as energy, gold and financials, but also a few brand new products. An example is the Claymore S&P/TSX CDN Preferred Share ETF, which holds a basket of preferred shares and is worth a look by anyone who wants a safe source of tax-advantaged dividend income for a non-registered portfolio. Another is the Amex-listed iShares iBoxx $ High Yield Corporate Bond Fund, which offers exposure to the U.S. junk bond market.

For all other ETFs, don't invest without first applying the following screening process suggested by Mr. Mordy, whose firm specializes in designing portfolios built from ETFs.

>>Strive for the lowest ownership costs. The cheapest ETFs have management expense ratios as low as 0.07 to 0.25 per cent, but some new ones are creeping up toward 1 per cent.

>>Watch the liquidity. Some ETFs don't trade much from day to day, which means it could be difficult to sell them.

>>Look at the index an ETF tracks. While most indexes weight stocks using a measure of size called market capitalization, several new ETFs track indexes using a so-called fundamental approach that throws in criteria such as dividend yield and cash flow. Mr. Mordy prefers the market cap, but is keeping an open mind about the fundamental approach.

>>Look for diversification. Make sure the holdings aren't dominated by a small group of stocks.

As busy as the ETF industry has been lately, it has a lot more for investors to look forward to. Prospectuses have been filed with U.S. regulators for new ETFs in such areas as dermatology and wound care, the Russian stock market and firms from 22 U.S. states. It will be interesting to see if the performance of these funds matches the creativity that went into devising them.

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