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Quant-Based ETFs In Focus

by [Michael Johnston](#) on December 30, 2011 | ETFs Mentioned: [CSD](#) • [FPX](#) • [FVL](#) • [KNOW](#) • [PEY](#) • [PKW](#) • [PWO](#) • [RYJ](#) • [tfs](#) • [WMW](#)

ETFs initially became popular with advisors and individual investors as tools for harnessing beta, allowing low cost ownership of broad equity markets through a vehicle that provided transparency, intraday liquidity, and potential tax efficiency to boot. The “first generation” of exchange-traded products were exclusively plain vanilla funds that targeted well known stock and bond benchmarks, such as the [S&P 500](#) or [Barclays Capital Aggregate Bond Index](#).

To the great delight of the pioneers of the ETF space, the last several years have seen ETF asset surge and adoption rates among all degrees of investors rise steadily; assets now top \$1 trillion, and ETFs often account for about a third of total trading activity. But to the great dismay of some of those pioneers, recent years have also seen ETFs become increasingly sophisticated and increasingly targeted; many of the new products debuting focus on narrow asset sub-classes of implement advanced screening techniques that seem to blur the lines between active and passive management.

Others have taken a much more positive view of this innovation; the advances made in recent years have given investors access to some complex but powerful tools that have the potential to generate excess returns relative to simple cap-weighted benchmarks. Specifically, there are a number of quant-based ETFs out there that use various factors to construct a universe of stocks backed by interesting—and sometimes compelling—investment theses [for more ETF insights, sign up for the [free ETFdb newsletter](#)]:

Direxion All Cap Insider Sentiment Shares ([KNOW](#))

This ETF is linked to an index consisting of 100 stocks selected from the broad-based S&P 1500 that exhibit positive insider sentiment. To measure the insider sentiment of a stock, the index considers publicly available information such as purchases and sales of company stock by employees or directors reported in SEC statement and changes to analyst outlooks for the company. The idea behind this approach is pretty straightforward: monitoring the activity of those closest to the company can provide some insights into the outlook going forward. If directors are buying up loads of shares and analysts boost their ratings or earnings expectations, it can be inferred that the “insiders” have a positive outlook. If directors are selling off shares and analysts who follow the company full time sour on the future prospects, the outlook might not be so bright [see [KNOW fact sheet](#)].

PowerShares High Dividend Achievers ETF ([PEY](#))

PowerShares’ PEY utilizes a dividend-focused investment strategy to provide investors with high current dividend income and capital appreciation at a relatively low level of risk. It achieves its objective by tracking the Dividend Achiever 50 index, which is designed to select stocks based on dividend yield and consistent

dividend growth. The resulting portfolio offers investors exposure to higher distribution yields than most broad-based market ETFs, making PEY an attractive option for investors wishing to enhance current returns in this low interest rate environment [see [PEY fact sheet](#)].

Guggenheim Raymond James SB-1 Equity ETF ([RYJ](#))

This ETF is one of the most interesting quant-based products on the market, offering investors exposure to a number of mid and small cap firms. RYJ utilizes a dynamic stock selection process that requires each security hold a Strong Buy 1 (SB-1) rating from Raymond James & Associates. The ratings are calculated based on a number of factors, including both quantitative analysis and analyst evaluation. Although this fund is classified as a passive ETF, the composition of its underlying portfolio is greatly influenced by human judgment and therefor its performance is also reliant on the accuracy of the Raymond James analysts [see [RYJ fact sheet](#)].

PowerShares Buyback Achievers ETF ([PKW](#))

PowerShares' PKW is linked to the Share BuyBack Achievers Index, which is comprised of U.S. companies that have repurchased at least 5% or more of outstanding shares during the trailing 12 months. Some investors are leery of stock buybacks since most would prefer excess capital to be paid out in dividends or used for company reinvestments. There is a general theory, however, that buybacks can actually help boost share prices if done at the correct time. The idea is quite simple: if a company buys back its stock, management believes that shares are undervalued. As such, sharebacks can also be seen as an indication of positive sentiment towards a stock, sending a signal to the market that the stock does in fact hold more value [see [PKW fact sheet](#)].

First Trust Value Line 100 ETF ([FVL](#))

This ETF seeks to replicate the Value Line 100 Index, a benchmark that is comprised of 100 securities that hold a #1 ranking in the Value line Timeliness Ranking System. Each week, the fund's underlying index is ranked based on a number of quantitative measures including proprietary calculations, such as long-term earnings and price trends, recent company earnings and price performance and earnings relative to expectations. Stocks which received high ratings in safety, performance, and most importantly, in timeliness are ranked as #1 while the worst stocks are ranked #5 [see [FVL fact sheet](#)].

Guggenheim Spin-Off ETF ([CSD](#))

CSD is the only ETF on the market that offers investors access to unique quantitative methodology that seeks to capture the performance of companies that have been spun-off within the last two years. Spin-offs are created by companies that have separated and sold off a portion of their business as a new entity. This process often times unlocks value: smaller, targeted companies are more flexible and can dedicate all of their resources towards their core operations, potentially allowing investors to capture the performance of a more efficient and profitable company. Some of CSD's top holdings include Ascent Capital Group Inc., Altisource Portfolio Solutions SA, and Philip Morris International Inc. [see [CSD fact sheet](#)].

PowerShares Dynamic OTC ETF ([PWO](#))

The Dynamic OTC ETF (PWO) is part of the PowerShares' suite of Intellidex funds, which utilize quantitative analysis to invest in various sectors of the U.S. equities market. This ETF seeks to replicated an index that is comprised of U.S. securities that exhibit the greatest potential for capital appreciation from each sector of the U.S. economy. The Intellidex methodology selects companies based on a number of quantitative measures such as fundamental growth, stock valuation, investment timeliness and risk factors. Although the fund in its nature is relatively broad based, the resulting portfolio is somewhat concentrated with only about 100 stocks that are currently biased towards the technology sector [see [PWO fact sheet](#)].

First Trust IPOX-100 Index Fund ([FPX](#))

This ETF offers investors exposure to companies that have recently undergone an Initial Public Offering (IPO) and are now available to the general public. FPX is linked to the IPOX-100 U.S. Index, a modified value-weighted price index that measures the performance of the top 100 IPOs during the first 1,000 trading days.

The fund uses a quantitative screening methodology to rank each IPO based on their market capitalization. It is worth noting that FPX generally does not participate in the first day “IPO pop,” since it will often establish a position shortly after a company becomes public. Still, focusing on recent IPOs can be an effective strategy if the capital raised during the process is used wisely and the enhanced visibility allows the company to improve profitability [see [FPX fact sheet](#)].

ELEMENTS Morningstar Wide Moat Focus ETN ([WMW](#))

This ETN offers investors exposure to securities of companies that have an competitive edge in their industry, or that Morningstar defines as having a “wide moat”. A wide-moat company is one that has a maintainable return on invested capital exceeding cost of capital and a sustainable competitive advantage. These firms are good for long term investments as they are typically stable firms that have either brand name power, high switching costs, or they are able to effectively prevent new entrants from competing in their industry [see [WMW fact sheet](#)].

AdvisorShares Trim Tabs Float Shrink ETF ([TTFS](#))

AdvisorShares’ TTFS seeks to outperform the Russell 3000 Index through the use of their TrimTabs methodology. The theory behind this methodology is that stocks perform best when the total number of outstanding shares has declined over the last 120 days. The idea is quite simple: if there is the same amount of money chasing a smaller number of shares, the price should rise. This methodology relies on corporate insiders timing buybacks based on information that may not be available to the general public. If this assumption is true, the stock repurchase is a signal to the market that the company has a bullish outlook on the prospects of their business [see [TTFS fact sheet](#)].

Disclosure: No positions at time of writing.

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