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Commentary: Global financials ETF outperforms

By Marvin Appel, Systems & Forecasts
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NEW YORK (S&F) -- Domestic financials have outpaced the rest of the stock market since last October and one exchar surpassed the U.S.-only financials.

I'm generally wary of sector funds because their potential investment risk is usually greater than that of the overall stock market Global Financial (IXG : **79.97**, **-0.17**, **-0.2%**) exchange-traded fund has had strong returns in the setting of below-average volat months.

IXG holds stocks in large money-center banks, insurance and diversified financial companies from around the world. Although t familiar American companies such as Citigroup and Bank of America, 130 out of the 220 stocks in the ETF are from foreign cor assets are invested in financial firms from outside the U.S.

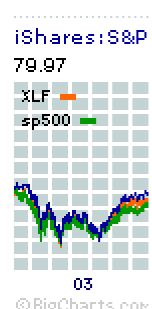
Financial stocks in general are attractive because the underlying companies are quite extremely profitable relative to their share world trade expanding and the development of capital markets in China, India and elsewhere around the world, multinational ba future prospects.

This particular ETF benefits from weakness in the U.S. dollar. When the dollar falls, the 58% of the portfolio that is valued in terı (mainly the euro, pound sterling and Japanese yen) becomes more valuable. The U.S. dollar has been weak for over four mont trade deficit.

In 2005, the negative effects of our trade deficit were overshadowed by the Federal Reserve's campaign to boost short term inte rates in the U.S. rise relative to rates abroad, the dollar becomes more attractive as a home for capital.) However, with the Fed's its end, and with other central banks beginning to raise rates elsewhere, the dollar has again become soft, to the benefit of the s

There is an important caveat regarding IXG. Although in the past year the volatility of IXG during market declines has been lowe & Poor's 500 Index, or than U.S. financial stocks, as represented by the Financial Sector SPDR (XLF : **32.61**, **+0.03**, **+0.1%**) , case. Specifically, in early 2003 it was more volatile than either the S&P 500 or than XLF.

You can appreciate this from the chart by noting that at the market low in March, 2003, IXG had sunk lower than the other two investments.



IXG did experience brief declines of some 7% in early 2006 even though its longer-term advance continues in place. This suggests that if you do wish to employ a trailing stock to control risk, the stop should be no closer than 10% below the current price.

In sum, IXG has the benefit of being in the midst of a strong advance, based on expanding opportunities for financial companies in the U.S. and abroad as well as favorable currency translations of the values of the underlying stocks. Overall risk is somewhat mitigated by the nature of financial companies as value stocks, with generally high underlying earnings serving as a potential moderating influence during periods of market decline.

Marvin Appel holds an academic doctorate in statistics. He applies his background in computer research and mathematical moc allocation strategies for the Systems and Forecasts newsletter. Appel has client accounts invested in IXG at the time of this writ (systemsandforecasts.com)

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