

Greening Your Portfolio with Green Exchange-Traded Funds

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It's been some 35 years since President Gerald Ford in his "State of the Union" address called on the U.S. to take steps to clean up the environment. Yet, it has taken decades before the initiative has gained enough traction among policymakers and the business community, both in the US and globally, to make it a paradigm for the new age of living clean and green. In line with this paradigm, and especially because of the surge in oil prices to record highs in recent years and the increasing incidence of environmental disasters associated with global warming, alternative energy production initiatives have come to the forefront of the global energy policy. Along with it has emerged a buoyant trend of investing in green energy companies. While there are many options to benefit from this trend, "greening" one's stock portfolio can be most effectively accomplished by investing in green Exchange-Traded Funds (ETFs).

Green ETFs represent a basket of alternative energy stocks that facilitate clean energy consumption through technologies that improve energy efficiency and reduce the adverse effect on the environment. The number and the appeal of these ETFs has surged in recent years, driven by the boom in global investments in **wind, solar, bio-fuel, and hybrid** energy production. For instance, new investments in clean energy production have risen 500 percent over the past five years, to \$145 billion in 2009. The outlook for capital growth in the sector is exceptional, with the combined global revenues for solar, wind, and bio-fuel energy companies expected to grow, on average, by 24 percent per year over the next decade. A carefully structured investment strategy can substantially benefit from this trend.

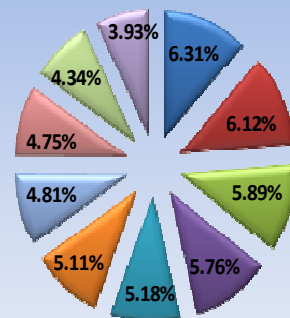
For example, by investing in green ETFs, long-term investors can supplement their core portfolio holdings to take advantage of the expected robust growth in the industry. This strategy can be used by investors who attempt to outperform the broader market over the long run. Given that green ETFs are usually well diversified across the industry, trading in them involves less risk than trading in individual stocks of the companies engaged in clean energy production. Moreover, investors can structure their holdings of green ETFs across the global markets or in a way that maximizes investors' exposure to trends in particular geographic regions or specific sectors within the industry.

Some green ETFs, such as *iShares S&P Global Clean Energy Index Fund* (NYSE: **ICLN**), invest broadly across international markets. **ICLN** invests some 80 percent of its assets in major international green energy companies, and 20 percent in the US-based enterprises. About half of the **ICLN** holdings are allocated to stocks of utility companies. The chart below summarizes the top ten holdings of this fund.



iShares S&P Global Clean Energy Index Fund **Holdings, September 2010**

- Energy Company of Parana ADR (ELP), Brazil
- National Electricity Company of Chile, Inc. ADR (EOC), Chile
- First Solar, Inc. (FSLR), United States
- Energy Company of Minas Gerais ADR (CIG), Brazil
- China Longyuan Power Group Corp Ltd (CLPXF), China
- Verbund AG (VER), Germany
- IberdrolaEnergias Renovables SA (IBR), Spain
- Vestas Wind Systems A/S (VWS), Denmark
- EDP Renovaveis SA (EDPR), Spain
- SunPower Corporation (SPWRA), United States



An example of a US-only green ETF is *PowerShares WilderHill Clean Energy Portfolio* (NYSE: **PBW**). Investors can also concentrate their green ETF holdings within specific sectors, depending on their expectations about performance of **solar, wind, biomass** or other energy producers. For example, *First Trust Global Wind Energy ETF* (NYSE: **FAN**) allows for a high exposure to the wind energy production while *Claymore Global Solar Energy ETF* (NYSE: **TAN**) provides for a high exposure to the trends in the solar energy production.

Summary

Adding green ETFs to one's investment portfolio does involve risks. Green ETFs only hold shares of companies engaged in the field of clean energy. This makes them more diversified than holdings of stocks of individual companies in the sector, but less diversified than general ETFs and the market as a whole. Therefore, green ETFs should constitute a relatively small share in long-term growth portfolios. These risks have to be put in the context of each individual's broad investment strategy.

As illustrated, there are several ways to structure one's portfolio in a way that may benefit from the global push toward a cleaner future. With global governments allocating more funds toward investments in the sector, green ETFs will gain in appeal. A prudent investment strategy that incorporates appropriate types of green ETFs can optimize investors' portfolios for successful long-term performance.

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