



Journal of Economic Perspectives

ISSN 0895-3309 (Print) | ISSN 1944-7965 (Online)

≡ Menu

Exchange-Traded Funds 101 for Economists

Martin Lettau

Ananth Madhavan

JOURNAL OF ECONOMIC PERSPECTIVES

VOL. 32, NO. 1, WINTER 2018

(pp. 135–54)

Download Full Text PDF
(Complimentary)

Article Information

Comments (0)

Abstract

Exchange-traded funds (ETFs) represent one of the most important financial innovations in decades. An ETF is an investment vehicle, with a specific architecture that typically seeks to track the performance of a specific index. The first US-listed ETF, the SPDR, was launched by State Street in January 1993 and seeks to track the S&P 500 index. It is still today the largest ETF by far, with assets of \$178 billion. Following the introduction of the SPDR, new ETFs were launched tracking broad domestic and

international indices, and more specialized sector, region, or country indexes. In recent years, ETFs have grown substantially in assets, diversity, and market significance, including substantially increasing in assets in bond ETFs and so-called smart-beta ETFs. Smart-beta strategies often used by actively traded mutual funds and hedge funds. In this paper, we begin by describing the structure and organization of exchange-traded funds, contrasting them with mutual funds, which are close relatives of exchange-traded funds, describing the differences

This website uses cookies.

By clicking the "Accept" button or continuing to browse our site, you agree to first-party and session-only cookies being stored on your device to enhance site navigation and analyze site performance and traffic. For more information on our use of cookies, please see our [Privacy Policy](#).

Accept

in how ETFs operate and their potential advantages in terms of liquidity, lower expenses, tax efficiency, and transparency. We then turn to concerns over whether the rise in ETFs may raise unexpected risks for investors or greater instability in financial markets. While concerns over financial fragility are worth serious consideration, some of the common concerns are overstated, and for others, a number of rules and practices are already in place that offer a substantial margin of safety.

Citation

Lettau, Martin, and Ananth Madhavan. 2018. "Exchange-Traded Funds 101 for Economists." *Journal of Economic Perspectives*, 32 (1): 135–54.

DOI: 10.1257/jep.32.1.135

Choose Format:



Additional Materials

[Online Appendix \(411.27 KB\)](#)

[Author Disclosure Statement\(s\) \(25.62 KB\)](#)

JEL Classification

G12 Asset Pricing; Trading Volume; Bond Interest Rates

G23 Pension Funds; Non-bank Financial Institutions; Financial Instruments; Institutional Investors

Copyright 2024 American Economic Association. All rights reserved.

[Terms of Use & Privacy Policy](#)

This website uses cookies.

By clicking the "Accept" button or continuing to browse our site, you agree to first-party and session-only cookies being stored on your device to enhance site navigation and analyze site performance and traffic. For more information on our use of cookies, please see our [Privacy Policy](#).

Accept