

THE ETF TRADER INTERVIEW SERIES: KATHRYN SWEENEY, GOLDMAN SACHS

Anita Rausch — Head of Capital Markets

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Welcome to the second installment of the ETF Trader Interview Series. In this edition, Anita Rausch, Director of Capital Markets, speaks with Kathryn Sweeney, the Global ETF Product Manager and Head of U.S. ETF Trading for Goldman Sachs. She joined Goldman Sachs in 1999 and moved to London, where she worked on the European ETF trading desk. In 2001, she returned to New York, where she traded international ETFs. She was named Managing Director in 2008. Kathryn earned a BA in Finance from Boston College in 1999.

AR: Tell us a little about yourself and your business. Let's start off by explaining your firm. Kathryn Sweeney: Goldman Sachs Group, Inc. is a leading global investment banking, securities and investment management firm that provides a wide range of financial services to a substantial and diversified client base that includes corporations, financial institutions, governments and high-net-worth individuals. **AR: What services do you provide? KS:** Goldman Sachs (GS) offers multiple services to our ETF clients. Within the firm's Securities Division, our global High Touch Sales and Trading desk works with large institutions, offering advice, solutions and capital. We make markets in ETFs across all asset classes and have been [a lead market maker](#) since the market's inception. We are a global leader in securities lending, providing prime brokerage and ETF lending services. **AR: Describe your client base and your experience. KS:** I have worked at GS my entire career, in both our NYC and London offices. Not only have I been at the same firm my entire career, but I have worked on the same desk for 14 years of my 15-year career. My experience is like most others at GS: client first, then the firm, then the desk, then the individual. We are structured to have a holistic approach when we deal with all clients. There is never the thought of one trade; we always think in terms of partnership. **AR: Give an example of a trading/execution strategy you have developed with a client. KS:** I will give an example of a strategy that helped a client in 2008. We had a client that was receiving a lot of redemptions from their portfolio; they wanted to move into ETFs so that they had more flexibility if they needed to raise cash. But their portfolio was global, and the ETF they were buying to replace that portfolio traded during U.S. hours. We worked a solution for the client, trading both their basket over a 24-hour period to pair cash flows from the sell portfolio and the inflows into the ETF. This minimized tracking and timing mismatches. Our global coordination allowed the client to get the exposure they wanted with the least amount of [slippage](#). They continue to use this strategy and now consider ETFs as a viable solution in their portfolio. **AR: What mistakes do you see clients making in their execution process? KS:** Benchmarking! Everyone has a benchmark, whether it is a mandated benchmark or one that your trading desk uses for execution. With ETFs, we are able to think outside traditional benchmarks. We always seem to work best when we are able to discuss the motivation for the trade and how we, as a desk, would think about execution. **AR: What do you wish you had available as an ETF trader that would help you and your clients? KS:** Transparency is key. I love when I have a conversation with a client and we discuss the intricacies of an ETF. With the innovation in the ETF market, it is important to understand what is inside each product. **AR: What do you wish clients would do better? KS:** Asking questions. ETF education is an ongoing process. With the growth in the ETF market—in terms of how products are structured and the underlying indices or baskets—it is important to understand what you are trading. **AR: How do you think ETF issuers could help the process of client execution and education? KS:** One of the biggest challenges we all have on ETF education is helping clients understand [liquidity](#). Essentially, how [authorized participants \(Aps\)](#) are able to interact with the primary market to increase liquidity in the ETF. This conversation becomes all the more important with new ETF product offerings that might not have much "on screen" liquidity. **AR: What do you think the future of ETF trading will look like? KS:** The ETF market has changed a lot in my 15-year career. I would never put a cap on what the ETF market will be able to achieve. Obviously, one major change has been that new product listings are directly related to client demand. The innovation in the ETF market has yet to see its peak. **AR: The ETF managed portfolio segment is one of the fastest growing segments of the ETF market. Is there anything in particular that group should be focused on when transitioning its portfolio holdings? KS:** This is a great question. I see two major issues that continually arise when dealing with any portfolio that is transitioning, whether it is an ETF managed portfolio or a stock portfolio: fragmentation

of orders and execution evaluation. We believe that it is best to look at every transition as a whole portfolio transition. Clients should consider how to allow for crossing opportunities in the underlying portfolio, how to trade ETFs where the underlying portfolios do not have similar market hours, and how to reduce execution fees and risk spreads. When the portfolio is broken into multiple trades, the portfolio manager might be introducing more slippage and fees than necessary. As for execution evaluation, we like to think about trades from a pre- and post-trade analysis. Focusing solely on the pre-trade analytics might lead a client toward a less-optimal benchmark and AP selection. **AR: Discuss the growth of the Fixed Income ETF segment and what you believe its effect on the bond market could be for individual bonds. KS:** I think of an ETF as a wrapper for an underlying product. When I am asked about Fixed Income ETFs and price discovery, I am reminded of when Emerging Market ETFs were first listed in the U.S. These ETFs became the barometer of price discovery for this space. The growth in these ETFs demanded that market makers figure out how to make this space more transparent and investable. That is what I see happening with Fixed Income ETFs. We are still in the early stages and look at the growth in both assets under management (AUM) and product offering. I expect more transparency to be driven because the ETF end client is demanding it. **AR: What is the best way to assess the potential liquidity of a fixed income ETF? KS:** This is a good question and difficult to have a one-size-fits-all answer. But generally, this is the way we think about liquidity: **Liquidity of an ETF = A percentage of Underlier Liquidity + ETF on-screen liquidity + hedges** With Fixed Income ETFs, the last piece of the equation, the hedges, becomes very important. **AR: What should clients be thinking about/asking when getting ready to execute an ETF block trade in a lower-volume ETF? KS:** They should think about the underlying liquidity and costs of trading in those markets. When trading large blocks, we like to talk to clients about how we view liquidity, the costs of trading and how to minimize these fees. Just asking for a risk market might not be the best approach. Our goal is to work within the client's benchmark, while being the most efficient in terms of slippage and fees. **AR: What are the most typical concerns you hear from clients regarding the ETF market? KS:** Two questions: Liquidity and how the creation and redemption process works. Clients want to make sure that we will be there when they want to get into an ETF and that we will be there if/when they need to get out. And they want to understand the process. **AR: Do you think the bid/ask spread, the difference between the best price you can buy and sell an ETF electronically, really matters when judging an ETF for investment candidacy? What do you think is the best way an investor should judge liquidity and execution cost of an ETF? KS:** The bid-to-ask spread shown electronically, typically referred to as "on-screen" markets does matter. While there are many ways to view the "fair value" of an ETF, the market price is the most common. But tight on-screen markets do not always mean that you can trade large risk at those levels, and wide on-screen markets do not always mean that the ETF is not tradable. When thinking about the liquidity and execution costs of an ETF, there are many things to consider—commissions, on-screen spread, underlying liquidity, stamp costs and the fees of creating and redeeming. Depending on the size of your order, each of these will be a factor in your decision process to a varying degree. **AR: Explain the significance of a creation unit. Do investors need to be aware of how many shares equal a creation unit for an ETF? KS:** Like in question 13, this will be a factor depending on the size of your order and the ETF. If the ETF has a lot of on-screen liquidity, then ETF creation size does not matter much. If the ETF you are trading does not have as much on-screen liquidity, then creation size becomes a factor. Always best to discuss with an AP. **AR: Thank you very much for participating in this series.**

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Lead Market Maker (LMM) : A broker-dealer firm that accepts the risk of holding a certain number of shares of a particular security in order to facilitate trading in that security.

Slippage : The difference between the expected price of conducting a transaction compared to the actual execution price.

Liquidity : The degree to which an asset or security can be bought or sold in the market without affecting the asset's price. Liquidity is characterized by a high level of trading activity. Assets that can be easily bought or sold are known as liquid asset.

Authorized Participant (AP) : An entity, usually an institutional investor, that submits orders to the ETF for the creation and redemption of ETF creation units.

Creation Unit (CU) : A specified number of shares issued by an exchange-traded fund (ETF) in large blocks, generally between 25,000 and 200,000 shares. The authorized participants that buy creation units either keep the ETF shares that make up the creation unit or sell all or part of them on a stock exchange.