Which NDX ETF is Right for You?

The Nasdaq-100 Index® (NDX®) is a modified capitalization weighted index that tracks 100 of the largest non-financial companies listed on the Nasdaq Stock Market. Today, ETFs across the globe – from the Americas and Europe to the Middle East and Asia-Pacific – track the NDX, making it one of the most popular indexes in the world. Each ETF is designed to track the NDX in a particular way, offering myriad opportunities for investors to incorporate them into their portfolios.

Cap-Weight vs. Equal Weight

Launched in March 1999, the **Invesco QQQ ETF** (QQQ) was the first ETF to begin tracking the NDX. As of September 20, 2022, QQQ had $159.39 billion in assets under management (AUM). Launched in October 2020, the **Invesco QQQ ETF** (QQQM), known as the Q mini, also tracks the Nasdaq-100. However, it has lower fees, a smaller share price and reinvests dividends, all of which may be more appealing to buy-and-hold investors.

The NDX currently has 102 constituent securities, spread across 101 unique companies listed on Nasdaq. (Note: the 101st company is temporarily included in the index as a result of a recent spinoff.) As of June 30, 2022, the top 10 companies represent about 52% of the total index weight, so they often, but not always, sway the direction of the index. The top two holdings – Apple (AAPL) and Microsoft (MSFT) – make up over 23% of the index. As such, NDX, and by extension QQQ, will naturally behave very much like its largest components.

The Nasdaq-100 Equal Weighted Index™ (NDXE™) tracks the same constituents, but it does not weight them by market capitalization. Instead, the index is equally weighted on the same quarterly rebalancing schedule as the NDX, bringing each company to a weighting of roughly 1%.

In April 2006, First Trust launched the **First Trust Nasdaq-100 Equal Weighted Index Fund** (QQEW), which tracks the equal-weighted version of the Nasdaq-100®, NDXE. As of September 20, 2022, QQEW has $1.08 billion in AUM.

QQQ is essentially the House of Representatives of the Nasdaq-100, treating AAPL in much the way that the state of California has an outsized voting contingent within Congress. QQEW is analogous to the U.S. Senate, where each state (read: company) has an equal number of votes.

Some other ETFs related to the NDXE include:
Direxion Nasdaq-100 Equal Weighted Shares (QQQE)
Invesco Nasdaq 100 Equal Weight Index ETF – CAD (QQEQ)
Invesco Nasdaq 100 Equal Weight Index ETF – CAD hedged (QQEQ.F)

Technology vs. Ex-Technology

The Nasdaq-100 inventory has always been tech heavy, but you'd be surprised to know some of the names included both historically and currently that are ex-Tech, such as Starbucks, that are included in the index.

In 2006-2007, First Trust added a pair of products to its ETF lineup that allowed investors to delineate Nasdaq-100 exposure along sector categories, specifically technology versus ex-technology. The viability of these products, which total nearly $2 billion in net assets between the two today, speaks to the growth that the Nasdaq-100 has continued to experience through tertiary products even as the index surpassed the ripe, old age of 37.

Launched in April 2006, the **First Trust Nasdaq-100 Technology Sector Fund** (QTEC) tracks the Nasdaq-100 Technology Sector Index™ (NDXT™), an equal-weighted basket of Nasdaq-100 components that are classified by ICB as part of the Technology industry. The fund currently holds 42 securities across the following subsectors within Technology: Software, Semiconductor, Production Technology Equipment, Consumer Digital Services, Computer Services and Computer Hardware. As of September 20, 2022, QTEC has around $1.6 billion in AUM.

Meanwhile, the **First Trust NASDAQ-100 ex-Technology Sector Index Fund** (QQXT) invests in the 60 other Nasdaq-100 companies, across the Consumer Discretionary, Health Care, Industrials, Consumer Staples, Telecommunications, Utilities and Basic Materials industries. It tracks the Nasdaq-100 Ex-Tech Sector Index™ (NDXX™) and employs an equal-weighted approach, as well. As of September 20, 2022, the fund has $126 million in AUM.

ESG Overlay

In October 2021, two new ETFs were launched to meet the demand for ETFs with an ESG overlay. The Invesco ESG Nasdaq-100 ETF (QQMG) tracks the Nasdaq-100 ESG Index™, and the Invesco ESG Nasdaq Next Gen 100 ETF (QQJG) tracks the Nasdaq Next Generation 100 ESG Index™. These investment products expanded the Invesco QQQ Innovation Suite to encompass a total of six products in the U.S. that include ETFs and other product wrappers.

Leveraged and Inverse ETFs

Some investors are interested in geared investing through leveraged and inverse ETFs. These products seek daily investment results, before fees and expenses, that correspond to the leveraged or inverse multiplier of the daily performance of the Nasdaq-100. ProShares offers five ETFs in the category: **ProShares UltraPro QQQ** (TQQQ) (+3x), **ProShares Ultra QQQ** (QLD) (+2x), **ProShares Short QQQ** (PSQ) (-1x), **ProShares UltraShort QQQ** (QID) (-2x), and **ProShares UltraPro Short** QQQ (SQQQ) (-3x).

Tracking the Trends

Launched in May 2021, the **ProShares Nasdaq-100 Dorsey Wright Momentum ETF** (QQQA) is the first ETF focusing on select Nasdaq-100 stocks identified as having the greatest potential to outperform based on their price momentum. Dorsey Wright, a recognized leader in momentum investing, selects the 21 leading Nasdaq-100 stocks based on a proprietary "Relative Strength" signal. Index constituents are assigned equal weights at every quarterly reconstitution in January, April, July and October.

The **Pacer Trendpilot 100 ETF** (PTNQ) tracks the Pacer Nasdaq-100 Trendpilot Index™, which borrows a concept from momentum investing to toggle allocations across NDX, T-bills or both. When the Nasdaq-100 Total Return Index™ (XNDX™) closes above its 200-day moving average price for five consecutive days, 100% of the fund's assets are allocated to (or remain in) NDX. When the Nasdaq-100 Total Return Index closes below its 200-day moving average price for five consecutive days, it invests only 50% in

NDX, and the remaining 50% in 3-month T-bills. 100% of the fund's assets are allocated to T-bills if the trend continues and the XNDX 200-day moving average itself finishes below where it was five days earlier. This would suggest a more sustained downtrend in market prices, so the fund opts to shift into full-on safety mode for downside protection.

Options-based Strategies

Investors may be looking to preserve upside exposure to NDX's stellar track record of growth and at the same time incorporate much-needed downside protection. A few passively and actively managed products may be used to hedge on the downside.

Global X offers five different Nasdaq-100 options-based index tracking ETFs.

- **The Global X Nasdaq-100 Covered Call ETF** (QYLD) is the most widely adopted of the five ETFs, with $6.71 billion in assets as of September 20, 2022. It also has the longest track record having launched in December 2013. QYLD tracks the CBOE Nasdaq-100 Buy/Write Index™, which holds Nasdaq-100 stocks and writes (sells) options simultaneously, generating option premium income that ends up in investors' accounts as a generous distribution yield. While not explicitly a downside protection strategy, QYLD functions as a more conservative income-generation vehicle, where more stable cash flows compensate for the diminished upside that investors receive from any price appreciation in NDX. The upside is capped directly because of the call options that the fund sells in the market.
- **The Global X Nasdaq 100 Covered Call & Growth ETF** (QYLG) follows a covered call or buy-write strategy. The fund buys the stocks in the NDX and writes (sells) corresponding call options on about 50% of the index. QYLG seeks to provide investment results that correspond generally to the price and yield performance, before fees and expenses, of the CBOE Nasdaq-100 Half BuyWrite V2 Index™.
- **The Global X Nasdaq 100 Risk Managed Income ETF** (QRMI) employs a protective net-credit collar strategy for investors seeking the income characteristics of a covered call fund, while mitigating the risks of a major market selloff with a protective put. QRMI seeks to achieve this outcome by owning the stocks in the NDX, while buying 5% out-of-the-money put options on NDX and selling at-the-money call options on the same index. QRMI seeks to provide investment results that correspond generally to the price and yield performance, before fees and expenses, of the Nasdaq-100 Monthly Net Credit Collar 95-100 Index™ (NQRMII™).
- **The Global X Nasdaq 100 Collar 95-110 ETF** (QCLR) employs a collar strategy for investors seeking range-bound equity returns. QCLR seeks to achieve this outcome by owning the stocks in the NDX, while buying 5% out-of-the-money put options on NDX and selling 10% out-of-the-money call options on the same index. The ETF's goal is to provide investment results that correspond generally to the price and yield performance, before fees and expenses, of the Nasdaq-100 Quarterly Collar 95-110 Index™ (NQCLRI™).
- **The Global X Nasdaq 100 Tail Risk ETF** (QTR) employs a protective put strategy for investors seeking to buffer against market selloffs. QTR seeks to achieve this outcome by owning the stocks in the Nasdaq 100 Index, coupled with buying 10% out-of-the-money put options on the NDX. The goal of the ETF is to provide investment results that correspond generally to the price and yield performance, before fees and expenses, of the Nasdaq-100 Quarterly Protective Put 90 Index™ (NQTRI™).

A few other ETF sponsors have issued ETFs that incorporate options strategies.

The **Nationwide Risk-Managed Income ETF** (NUSI) is an actively managed fund that utilizes an options collar; however, it is in conjunction with actual investment in the NDX. NUSI resets monthly and approximates what would be considered closest to a "truly hedged" ongoing investment in the NDX. By writing calls, some upside is limited, but the downside protection from puts is paid for upfront. Since it is actively managed, it will generate an income yield for investors if the manager does not fully convert the proceeds from selling call options during a given monthly period into new puts.

The **JPMorgan Nasdaq Equity Premium Income ETF** (JEPQ) is an actively managed portfolio that provides exposure to and resembles the NDX. The investment philosophy is to select securities of innovative large-cap companies that will likely outperform the NDX and will likely generate a modest amount of alpha based on a proprietary fundamental framework. At the same time, it avoids selecting stocks that have greater left tail risk or extreme downside performance periods. Investors receive the dividend associated with the long portfolio as well as the income generated from selling out-of-the-money options on the NDX. In addition, they may get some upside benefit when the market moves higher. The fund's goal is to achieve a diversified source of return and consistent monthly distributable income, although the return is not guaranteed.

First Trust offers four buffer ETFs – **First Trust CBOE Vest Nasdaq-100® Buffer ETF** (QMAR, QJUN, QSPT, QDEC) – that use FLEX Options to employ a target outcome strategy, which seeks to produce pre-determined investment outcomes based upon the performance of an underlying security or index. The fund seeks to provide returns that match the price return of the Invesco QQQ Trust up to a predetermined upside cap as well as a buffer against a certain amount of underlying ETF losses.

The **Simplify Nasdaq-100 PLUS Convexity ETF** (QQC) seeks to provide capital appreciation by tracking the large-cap U.S. growth stocks in the NDX. At the same time, it aims to boost performance during extreme market moves up or down via a systematic options overlay, which helps to create convexity in the fund. Convex investment strategies are expected to be highly correlated with the benchmark in typical market environments but diverge to the positive in extreme markets. Further, convex strategies are expected to lag during quiet markets.

The **Simplify Nasdaq-100 PLUS Downside Convexity ETF** (QQD) seeks to provide capital appreciation by tracking the NDX. A modest option overlay budget is then deployed into a series of options positions that help create downside convexity in the fund.

The **STF Tactical Growth ETF** (TUG) is an active, rules-driven fund that seeks long-term growth of capital with downside mitigation. The **STF Tactical Growth and Income ETF** (TUGN) ETF seeks long-term growth of capital in addition to monthly income with downside mitigation. Both ETFs seek to reduce equity exposure in bearish market environments while remaining invested during bullish market environments.

The funds' advisor utilizes a proprietary method called the Tactical Unconstrained Growth (TUG) Model to manage the funds. The TUG signal determines exposure to the Nasdaq-100 Index, long duration treasury bonds or treasury bills based on market trends and volatility. The ETF vehicle allows for tax efficient pivots between equities and bonds.

With TUGN, an options overlay seeks to generate monthly income and potentially enhance returns. The fund may sell call options on the NDX on up to 100% of the value of the equity securities held by the fund to generate premium from such options. At the same time, it may reinvest a portion of the premium to buy call options on the same reference asset(s).

Summary

The number of ETFs that track the Nasdaq-100 continues to grow, providing the opportunity to create customized investment strategies that leverage the unique sector and thematic exposures of the index in various ways. Among the multiple products that now exist, investors can toggle their NDX exposure with active vs. passive management, market cap vs. equal weighting, sector constraints, risk protection (especially on the downside), and/or targeted return (income). Financial advisors are encouraged to learn more about the ETFs that track the NDX and how they can be used within their clients' portfolios.

Sources: Nasdaq, FactSet, Bloomberg.