3 Sector-Specific ETFs to Consider in 2022

Description

Diversification: it's a powerful tool against market headwinds. But it's important to understand that just as too little diversification can be crippling for your portfolio, too much diversification can also have adverse effects. It can dilute the return potential of your capital.

One way to maintain the right balance between over and under diversification is to invest in sector-specific ETFs. They offer some measure of diversification (different companies within the same sector), but they also offer other benefits. The narrow exposure of sector-specific ETFs can be helpful if you want to beat the market long term or during specific downturn phases.

A banking-specific ETF

RBC Canadian Bank Yield Index ETF (TSX:RBNK) is a banking-specific ETF from, ironically, the largest bank in Canada. The idea behind the index is that the ETF tracks are following the performance of the Big Six bank stocks in Canada as closely as possible.

It only has six holdings; however, the weight distribution leans more heavily towards the yields rather than the market cap. The three largest holdings (by weight) are **Bank of Nova Scotia**, **CIBC**, and **National Bank of Canada**.

Collectively, the three make up over two-thirds of the entire weight (67%) of the ETF. The fund makes monthly distributions, and the payouts have slowly grown over the years. The MER is modestly high at 0.33%, and the fund carries a medium- to high-risk rating, owing to a relatively small basket of securities it follows.

A REIT-specific ETF

Another ETF that focuses on the Canadian market elements is **FTSE Canadian Capped REIT Index ETF** (TSX:VRE). The ETF offers you exposure to the Canadian real estate market, as evident from the name.

It's currently made up of 18 different stocks, most of which are REITs, but there are other real estate companies. The strong growth potential of stocks like **Colliers** and **FirstService**, both of which are in the top 10, has influenced their performance.

If you had invested $10,000 in the fund about 10 years ago (Nov. 2012 to inception), you would have grown it to about $18,900. And that's after the decline the ETF is currently experiencing. It also offers monthly dividends, and the current yield is relatively healthy at 3.14%. It comes with an MER of 0.38%, which is a bit high, but it also follows a more diversified basket of assets than the banking ETF.

A healthcare ETF

The healthcare sector in Canada has been underperforming the market for quite some time, thanks mostly to the marijuana industry bust. So, if you are looking for an ETF in this sector, going across the border might be a brilliant idea.

BMO Equal Weight US Health Care (Hedged to CAD) Index ETF (TSX:ZHU) follows the performance of a large set of companies: 73. That's quite significant for a sector-specific ETF.

All the companies are located in the U.S., and there is a lot of diversification within the sector. Healthcare equipment companies dominate the ETF (by weight), which is a nice change of pace compared to the pharmaceutical-heavy baskets of securities.

The ETF makes annual distributions, and the yield is paltry. It also carries the highest MER of the three (0.4%), but it's pretty justified considering its performance, which seems to double your capital in a decade.

Foolish takeaway

The three ETFs have their own levels of diversification. The Canadian banking one is the least diversified, and the U.S. healthcare one is the best in this regard. However, all three offer you impactful exposure to the underlying sectors, and if you understand the dynamics of these sectors, you can make smart investment decisions regarding these ETFs.

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