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PowerShares New Alternative Energy ETF's

Richard Kang submits: PowerShares has finally launched the ETFs that take choices for alternative energy beyond PBW in this space.

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For investors in PBW, the new cleantech fund and the progressive energy fund may be a bit of overkill in terms of holding all three. First let's review PBW:

PBW peaked at just under 24 in early May ending a 50% rise since the beginning of 2006. Wow. However, like all of the energy complex it fell hard this summer. PBW had a drawdown of roughly 30% hitting lows around 16.30 in late September. In fact, since September 22nd, PBW has risen about 13% to October 16th. A pull back in the past week and a half to just under 18 at the time of writing makes this look like a good point to get in. Recent action can't be considered evidence of the beginning of a longer term uptrend but we're still in a much better valuation than we were in early May.

PBW holds a diverse portfolio of 42 stocks with the largest sector weightings in IT (37%) and industrials (29%). Although it holds a small number of relatively "clean" utility companies, I consider this fund as a Nasdaq play on stocks with an alternative investment bent. I see alternative energy as a new technological wave commonly seen in major Nasdaq uptrends. Tech waves in the past have come in different forms but are clearly based on new innovations such as the biotech/pharmaceutical wave and the telecommunications/internet wave. On the positive side for alternative energy, we're nowhere near the speculative state of the dot com bubble. But with 42 stocks and a small cap growth bias, this fund is significantly more volatile than the Nasdaq which is a volatile index itself! Based on this kind of volatility, PBW shouldn't comprise any more than 5% of a portfolio.

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In the case of PUW, the fund is based on the WilderHill Progressive Energy Index. "The Index is comprised U.S.-listed companies that are significantly involved in transitional energy bridge technologies, with an emphasis on improving the use of fossil fuels. The modified equal-weighted portfolio is rebalanced and reconstituted quarterly."

Again, I find it interesting to find another ETF moving away from market cap weighted indexation. This continues the trend started with RSP (Rydex S&P Equal Weighted Fund) and furthered today by firms like PowerShares, Claymore and WisdomTree. Although not an ETF manufacturer, I always try not to forget Dimensional Fund Advisors, the pioneer in the space of non-market cap weighted passive funds.

Looking at the stats on this ETF (sector weights, underlying holdings dispersion by market cap, etc.) I find it to be the most unique, or at least significantly different in its composition compared to PBW and PZD. I would guess that this would be the least volatile of the three. Despite this assumption, again I have to state clearly it would still be significantly more volatile then the Nasdaq.

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I still believe that these funds will have strong correlations with the commodity indices, especially with the strong bias in these for energy. Like energy, these will be volatile so I can't think of holding any combination of these in a sum of more than 5% in a portfolio.

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