Exchange-Traded Funds

The Latest ETF Tracks Natural Gas Futures

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Yet another commodity exchange traded fund recently hit the ETF market: the **United States Natural Gas Fund**. (UNG)

It's the first pure natural-gas ETF, tracking the near two-month natgas futures contract. The percentage changes in the fund's value aim to reflect the percentage changes in the price of natural gas delivered at Henry Hub in Louisiana as reflected by the futures price changes.

"There's been exposure available in commodity-related ETFs to natural gas before, but this is the first one that focuses specifically on natural gas," said Scott Ebner, senior vice president of the Amex ETF Marketplace.

It's not the fund's intent to have an NAV being equal, in dollar terms, to the dollar price of spot natural gas or any particular futures contract based on natural gas.

Convenient Trading

"We've definitely in the past several years seen a very strong trend toward offering a broad variety of commodity exposure in ETF vehicles," Ebner said.

"There's a convenience factor to being able to own a product where a manager is now going to take care of the process," he said. "Futures expire and then you have to roll into the next one when investing in commodity futures."

Deron Wagner, founder of Morpheus Trading Group, says that the fund is a good idea for the average retail investor:

"I would agree that institutions don't have much of the demand for it because they can just trade the actual (futures) contracts.

"But for your average retail investor, that's a lot of complication and additional expense. They have to open a different account and they can't do that in an IRA, for example, whereas this can be traded with the same simplicity as a stock."

The total fees of the fund are expected to be 77 basis points.

Tracking Error

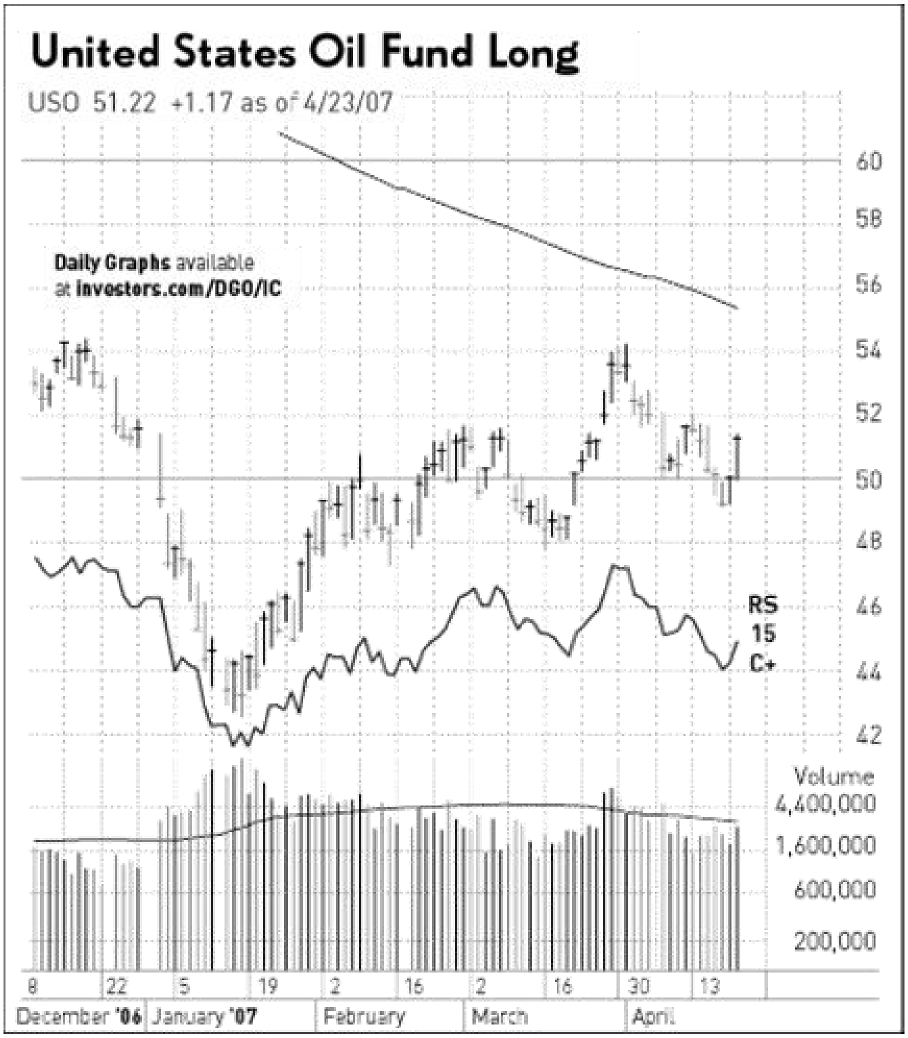
J. Mark Spallanzani, managing partner at Alcott Capital Management, believes investors need to be careful about the potential tracking error of the fund vs. the underlying commodity. In recent months, the performance of several commodity ETFs strayed away from the performance of the underlying products.

"We have to watch the volume and tracking error of UNG before we commit clients' money to it," said Spallanzani. "In the meantime, we would rather get the same exposure in the futures and options market."

Ebner also points to the fact that the risk of the underlying commodity exposure remains. Natural gas tends to be very volatile.

However, retail investors can use the fund as an alternative or an additional tool to add a small portion of the commodity to their portfolios.

"The thing that I've found is that there's a lot of divergence sometimes between the price of natural gas and oil," said Wagner. "The more opportunities people have to trade exactly what's showing the most strength, the better choices people have.



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