

Trading and liquidity

A deeper dive into exchange-traded funds

In the world of exchange-traded funds (ETFs), understanding liquidity isn't just a technical detail—it's the key to unlocking efficient execution, accessing broader opportunities, and potentially improving execution outcomes for investors. This guide equips you with the knowledge and language to navigate ETF liquidity with confidence—and to make informed, strategic trading decisions.



Truly understanding ETF liquidity and avoiding common pitfalls

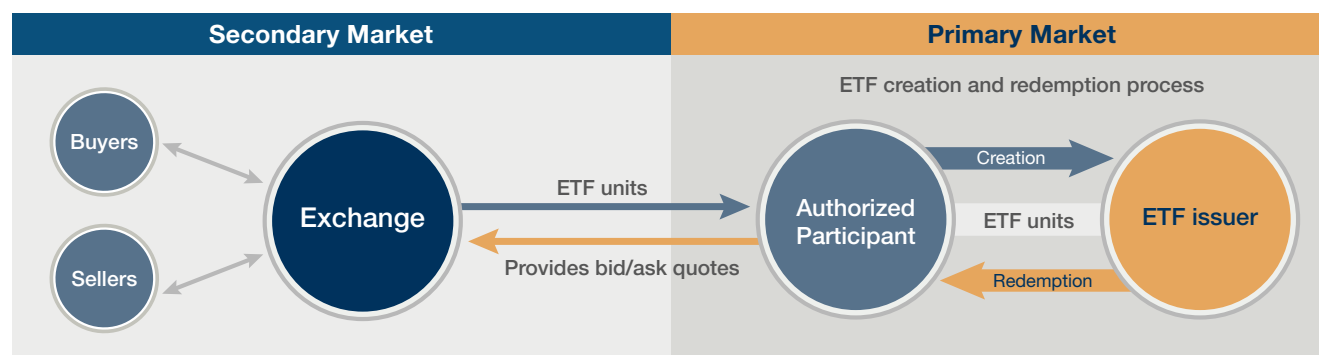
ETF liquidity is often misjudged when based solely on average daily volume (ADV) or bid-ask spreads. While these metrics describe secondary market activity, they don't tell the whole story.

ETF liquidity has two layers:

- **Primary Market Liquidity.** The ability of Authorized Participants (APs) to create or redeem ETF shares based on the liquidity of the ETF's underlying holdings.
- **Secondary Market Liquidity.** The buying and selling of ETF shares between investors on an exchange.

Key Point: An ETF with low daily volume can still handle large trades efficiently if its underlying basket consists of liquid securities.

ETF liquidity: example of the primary and secondary market process



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True liquidity

The true liquidity of an ETF is driven by the liquidity of the stocks (or other securities) held in the Fund's portfolio, also known as the underlying basket. Consider the structure of the product: an ETF is a basket of securities divided into shares that trade on an exchange. When an investor buys a share of an ETF, they are effectively purchasing a portion of each of those stocks—in some cases, hundreds of stocks at once—with a single trade. The ETF's liquidity can be accurately measured by the liquidity of the contents of that basket.

Example: Imagine you see an ETF with an ADV of 105,000 shares. At first glance, it seems modest. But upon closer look, you discover it could handle up to 45 million shares because its holdings are actively traded. That's the power of true liquidity.

Why does it matter? Although screen volume may be low, the ETF remains efficiently tradable because market makers can use the creation and redemption process to manage liquidity.

Myths that could cost you—and the truth behind them

Myth	Reality
Low average daily volume (ADV) means the ETF is illiquid	True liquidity depends on the underlying securities and the creation and redemption process—not just on-screen volume. Authorized Participants (APs) create and redeem shares continuously to support efficient trading.
The best time to trade an ETF is at market open or close	Midday, between 10:00 am–3:30 pm (ET), typically offers better spreads and stability.
ETFs with higher levels of assets under management (AUM) guarantee better execution	Smaller ETFs can be highly liquid if their holdings are liquid and supported by an active creation and redemption process. Many niche or specialized ETFs trade large institutional blocks daily even when on-screen volume is low or zero.
The last traded price equals fair value	Real-time bid/ask quotes better reflect fair value than the last traded price, which only shows the last transaction.



Four proven ways to trade ETFs smarter

- 1. Use limit orders.** To help control execution price and avoid unexpected order fills.
- 2. Trade during midday hours.** Spreads are typically tighter once underlying markets are fully open and before the close.
- 3. Look at underlying liquidity, not just ADV.** An ETF's true liquidity comes from its underlying basket, not just the average daily volume of ETF shares.
- 4. Monitor bid–ask spreads and timing.** Entering trades when markets are stable and spreads are tight improves execution quality.

When you can confidently understand ETF liquidity mechanics and move more efficiently through execution strategies, you not only can improve trade outcomes, but strengthen trust in your investment approach.

Knowledge of true liquidity, while collaborating with trading experts, positions you as a confident, informed investor who can potentially expand portfolio possibilities.

Execution guidance for large trades

We recommend using a Request for Quote (RFQ) process to access deep liquidity and competitive pricing. Advisors can ask their trading desk to conduct RFQs, which allows the desk to reach out to multiple liquidity providers on their behalf. Our Capital Markets Desk can assist by providing introductions and contact information to help facilitate this access.

Your Capital Markets Advantage

Our Capital Markets Desk acts as your trading resource—offering insights and connections you need for efficient execution.

- **Trade smarter** — Pre-trade guidance on timing, order type, and market conditions.
- **Access liquidity** — Relationships with multiple market makers to help source liquidity.
- **Educate clients** — Resources to simplify ETF trading and strengthen client conversations.

Execute with confidence

Whether you're navigating a large trade or exploring the right investment structure for your portfolio, we're here to help you trade with confidence.

Capital Markets Desk

Call: **212-576-8247** or **212-576-6070**

Email: **trading@nylinvestments.com**

Visit our website at: **newyorklifeinvestments.com/etf**

The average volume of a security over a longer time period is the total amount traded in that period, divided by the length of that period. Therefore, the unit of measurement for average volume is shares per unit of time, typically per day. **Liquidity** describes the degree to which an asset or security can be quickly bought or sold in the market without affecting the asset's price. **Liquidity risk** is the risk that certain securities may be difficult or impossible to sell at the time that the seller would like or at the price that the seller believes the security is currently worth.



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This material has been developed to meet the needs of financial intermediaries.

Examples are for illustrative purposes only and not indicative of future trading capacity. Past performance is no guarantee of future results. Execution efficiency does not guarantee better investment outcomes. Trading ETFs involves risks, including possible loss of principal. Market conditions can impact liquidity and execution quality.

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