

Transcript

The Ideas Exchange

Episode 32: Exchange Traded Products - outlook and opportunities

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**Jacinta King (00:01):**

Welcome to The Ideas Exchange by ASX, connecting you with investment experts, market updates and ideas. My name is Jacinta King, and I'm your host. This is our regular podcast covering everything from investment trends through to different ways to invest using a variety of products.

**Disclaimer (00:19):**

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**Jacinta King (00:47):** Hello, and welcome to The Ideas Exchange. My name is Jacinta King, and I'm your host. iShares has been a leader in the ETF marketplace for more than two decade, and as a part of BlackRock, their products are engineered by investment professionals with discipline and deep risk management expertise. Today, Tamara Haban-Beer Stats joins me from iShares where she leads the ETF and Index Investments Specialist Team. Welcome, Tamara.

**Tamara Haban-Beer Stats (01:12):**

Pleasure to be here, Jacinta.

**Jacinta King (01:13):**

It's great to have you because you've got some amazing background and insights, and we are going to get to that, 'cause I do want to hear about what has brought you to the work that you do at iShares. But firstly, I wanted to introduce for people we're going to discuss a couple of things today. We're going to look at the growth of ETFs, market insights from iShare's mid-year outlook, and some common questions about ETFs. So before we head into those, I want to know a bit more about you. So can you start by telling us about your background and the work that you do at iShares?

**Tamara Haban-Beer Stats (01:41):**

Sure, Jacinta. Well, I work, as you mentioned, at BlackRock in the iShares business, and I lead the ETF and Index Investments Specialist Team. As specialists, we work really closely with a number of our partners within the firm, particularly the wealth and institutional client business teams where we help clients navigate the growing choice in the ETF world. We also work on specific portfolio construction queries, and we help with implementation discussions. We also connect clients with our broader capital markets team for larger trades. We also spend a fair bit of time on what I would describe as advocacy. So where we broadly help everyone understand the growing use cases for ETFs, whether they're institutions, advisors, high net worth clients, family offices, or indeed, people such as you and I. We work really closely with partners as well that have the reach to retail investors such as yourself to center. So I joined BlackRock two years ago from investment banking, seven years at J.P. Morgan and about the same at Deutsche Bank before that.

**Jacinta King (02:44):**

You started there as a graduate, I believe.

**Tamara Haban-Beer Stats (02:46):**

As a graduate, just two formal workplaces before BlackRock that both Deutsche and J.P. Morgan I helped corporate clients around Australia with risk management strategies using derivatives.

**Jacinta King (02:58):**

I'd argue a good foundation, though. Tapping into that, you were talking about advocacy just before, so in your LinkedIn profile, you've noted your areas of interest and expertise as markets, strategy, sustainability, but you also, you put there democratizing investing. So I was really interested in that. Can you please share for us what you mean by democratizing investing?

**Tamara Haban-Beer Stats (03:16):**

Sure. I actually added that last pillar, I suppose, to my profile not that long ago because it's something that I feel really strongly about. BlackRock's purpose is really to provide more and more people with tools to promote their financial well-being. When I joined the iShares business, predominantly the ETF business, there I found the ultimate tool in democratizing investing. So they're just fantastic ways for everyone in the investment community to access opportunities and exposures in a really accessible, transparent, cost-effective way. So democratizing investing is something that BlackRock feels really strongly about as one of our core purposes, and it's one of my core purposes as well. We're trying to bring the investment opportunities to as many people as possible.

**Jacinta King (04:01):**

A good alignment there on your personal and professional interests. Earlier this year it was stated in the Australian Financial Review that the local ETF, so that's the exchange-traded fund market, will triple in size from U.S. 100 billion to U.S. 300 billion by 2027, so that's not far away. In Australian dollars that's 145.4 billion to 435 billion. So what do iShares think of this projected growth and some of the drivers of this?

**Tamara Haban-Beer Stats (04:28):**

Yeah, I think that's a great point, Jacinta. I certainly think that the growing understanding of ETFs and what they are, so exchange-traded funds as you mentioned, and that the fact that they're an accessible way to invest particularly into exposures that maybe investors didn't know how to get access to, for example, international exposures and particular sectors, and the fact that they give you all of the benefits of diversification and remove that idiosyncratic single stock risk. So I definitely think that is a factor, so a growing understanding. Then when I think about what's happened in the rest of the world, I certainly think that the penetration rates in Australia are relatively low compared to markets such as the United States and as well as Europe.

So when we look at the percentage of ETFs used in equity markets, in Australia, it's circa 5% and maybe a little bit under. When we compare that to the United States, that figure is upwards of around 12, 13%. When we look at fixed income, it's even lower. So here it's less than 2%. So less than 2% of fixed income investments are made using ETFs. Whereas, in the United States and places like Europe as well, it's much higher. So in Europe the number, I think around 10% of equity investments are made. So when you compare 4 or 5% to 10% or 13% in the U.S., you can see that we've got a fairly long runway, and we think that that gap will narrow. One of the things that I think is really driving that is the evolution of fixed income ETFs. So that is an asset class that has historically been not that well understood by investors, and it's often been the domain of specialist investors.

So it has brought, I guess, a new asset class to more people and more investors. I think that the evolution of fixed income will continue to drive a lot of growth, and we have seen a lot of flow into fixed income ETFs over the course of 2023. Another key driver is the growth of what we call model portfolios. So if some of your listeners are advised by a financial advisor, you might be invested into what's called a model portfolio across asset classes. So it's a multi-asset solution and we think the fact that they are an efficient way for advisors to manage their client portfolios, the building blocks that often go into those model portfolios are ETFs.

So the growth of model portfolios, and by virtue of that, the underlying building blocks being ETFs I think will also be another driver of ETF growth in Australia. Then finally the other thing that I'd mentioned, Jacinta, is just that new wave of investors where there's improved access to financial literacy and education through things like social media as well as other forums, we think that the growing understanding from overall has increased and will continue to increase. Not to say that there's not a ways to go, of course, and we believe that through sharing insights and education through our own website and publications as well as partnering with people like yourself, we certainly hope to grow the overall understanding of the ETF landscape and the opportunity that it provides.

**Jacinta King (07:31):**

Yeah. Well, this is the indicators that we're seeing at the ASX too with the number of... we had a record listing last year, I think it was around 42 products, and we're tracking pretty close to that and may even end the year a little bit more than that. So it's pretty exciting space for us as well. I also resonate with you with what I like about the work I do is that education component and helping people understand how ETPs fit into investments.

**Tamara Haban-Beer Stats (07:58):**

Absolutely. I guess we are starting to see that new wave of investors come through, and I think part of that is because of the financial education that's more prolific out there, particularly through forums like this one and the work that you have on your website. We also try and provide a lot of educational materials on our own website. We've also been prolific this year in terms of our product development, so I think that statistic is not unachievable at all.

**Jacinta King (08:26):**

Interesting, so watch this space. Now I want to shift to the mid-year outlook that iShares published at the end of June, and there are three takeaways which I'd like to discuss with you as I provide investors some good food for thought. Now the three things there was Holding Tight, Pivoting to New Opportunities and Mega-Forces, Mega Soon, so interesting titles there. So we will delve into Holding Tight so higher for longer interest rates. I'll give it a context there. I was at a seminar yesterday and naturally there was discussion on interest rates, and we can't forecast, who can?

But people were in the camp of rates will hold in Australia. Some said maybe it might actually go up, there might be one more. There were a few contrarians who said, "No, no, I think they might drop down." But the consensus seemed to be in the room that interest rates are higher for longer interest rates here to stay at the moment. So supporting

allocations to high-quality fixed income is what is noted here from iShares. For me, bonds come to mind. So how might an investor approach their portfolio when considering higher for longer interest rates?

**Tamara Haban-Beer Stats (09:35):**

Well, I think you hit the nail on the head there, Jacinta. That is our number one investment theme, so Holding Tight and we've seen around the world, I don't think another person needs to explain the pace and the aggressiveness of rate hikes around the developed world. But I think we're now definitely in a phase where the impact of those higher interest rates, so monetary policy that's been enacted by central banks, we're in that period where we're seeing how that plays out. Whether there's one more, no more, more than one more, we don't know, but our view is that we don't think that rates will be cut anytime soon. So we do think that central banks will keep interest rates in restrictive monetary policy for some time. As that relates to investments, how can you take advantage of that particular environment, which is indeed a very different environment to that that we've seen in the last several decades. We think fixed income. So fixed income is a hugely growing sphere and there's a lot of different types of fixed income.

So we really do think that there are opportunities, particularly in the front end of the curve at the moment when you look at where yields are, given that aggressive pace and size of monetary hiking, do definitely think that the short duration fixed income exposures makes sense. That said, we do think that there are other opportunities in the other parts of the fixed income market, and we've seen the data that demonstrates that as well. So 2023 for us as an iShares business, as a global business has definitely been a year of fixed income, so the flows have roughly doubled. So the net flows, so after all the ins, all of the outs, it's roughly double the size of the equity. There is also one of the points you made earlier, Jacinta, was education. I think a lot of people historically hadn't necessarily understood fixed income particularly well, and that's started to change. So we think that more investors have looked far more closely at their fixed income allocations, and we've seen people allocate towards, I guess what has historically been described as a defensive asset class.

**Jacinta King (11:40):**

Now your second theme in the mid-year report was Pivoting to New Opportunities. So I'd say that many of us are getting used to this term pivoting. So in the context of this conversation, though, what are some of the opportunities iShares are seeing at the moment?

**Tamara Haban-Beer Stats (11:53):**

Well, sticking for a moment on fixed income because I think there are opportunities within the fixed income market as well, I already mentioned, and we're seeing quite a lot of interest in the front end of the yield curve. But we're also seeing quite a lot of interest in our inflation linked fixed income products that's globally, not just locally, so particular styles of fixed income. So inflation-linked bonds are very popular. But that said, I think the opportunities also still extend to equity markets. We already talked about how we believe that the macroeconomic regime now in the world and all around the world is fundamentally different to what we've previously experienced, so that structurally higher level of rates and persistent inflation. There's a few reasons for that that I can go into, but namely, the rewiring of supply chains. The transition to a lower carbon economy are a couple of those things, worker shortages or supply shortages are another reason.

But when you think of all of those things that are happening in the macroeconomy, kind of sounds a bit negative, it sounds a bit tricky. But I think we absolutely, fundamentally believe that in this particular environment there are still those opportunities that are available, so pivoting to more granular, sectoral specific opportunities or specific parts of the fixed income market, which we already spoke about. So a couple of examples I can give are infrastructure. We really like infrastructure. We think it's a sector that's poised to take advantage of that shift to a lower carbon economy. It's also one of those essential services, so waste and water services, energy transmission and distribution, we think that this particular sector is an opportunity to invest in now. It also capitalizes on that first theme around Holding Tight when we think of the inflation pressures because a lot of the infrastructure assets and exposures that you can invest in do have explicit CPI linkages, which does add more of that ballast to investor portfolios.

**Jacinta King (13:56):**

Yeah, so it's essential services that no matter what is happening in markets, people still need them and will be using them and as you mentioned, the CPI linkage there. So thirdly, the media report also stated Mega-Forces, Mega Soon, so you're talking here about demographics and artificial intelligence impacting present-day returns. I find that AI stuff really interesting. So can you elaborate on this key takeaway for us?

**Tamara Haban-Beer Stats (14:20):**

Sure. So mega-forces, we've identified as a firm five mega-forces. So the changing nature of demographics around the world and artificial intelligence and digitalization are just two of them, but there's certainly ones that we can talk about today. So artificial intelligence is an opportunity that we've seen really come to the fore in 2023. Markets

have seen that in the performance of indices such as the S&P 500 over the course of this year where the drivers of performance were very much linked to some of those technology stocks that we're able to capitalize on and what's happening in the artificial intelligence space. We think that that opportunity in artificial intelligence is starting to broaden, so broaden out from companies that are direct beneficiaries, i. e., those that have the associated hardware to those that are in sectors who are able to best, I guess, capitalize on the technology itself from a productivity sense, an opportunity now and into the future as well.

Demographics was the other one and changing demographics, so there is an amazing statistic. So we calculate that by 2050, there'll be over 426 million people globally aged over 80 years old. So we're seeing as a proportion of the overall population, unless you're still working at that stage, we are starting to see that the number of working people as a proportion of the overall population is declining and that the older members of society are increasing. So we think that healthcare and healthcare innovation is a really great way to, I guess, take advantage of that particular mega-force.

We know that the demand for healthcare often increases as people do age. So we think that healthcare has one of those qualities that has a fundamental driver of demand, but also has an inelasticity of demand in many cases, particularly when we think about the inflationary environment. But the other really interesting reason why we like healthcare is because it's also at the forefront of technological innovation. When we look at what's happened with mRNAs and Messenger RNA, which was one of the driving forces behind some of the vaccines that we recently saw, the application of mRNA technology has now been expanded to treating other health issues such as Alzheimer's and Parkinson's disease. So healthcare remains one of our highest conviction calls, and it is that really nice, I guess, combination of both defensive as well as innovative sectors.

**Jacinta King (16:57):**

Excellent. Thank you for that great wrap up and overview of the mid-year outlook. Before we finish today, I actually wanted to ask you, what are some of the common questions about ETFs that you've found in your work?

**Tamara Haban-Beer Stats (17:09):**

Well, Jacinta, we still often get, "What is an ETF?" Believe it or not.

**Jacinta King (17:14):**

I do too, yeah.

**Tamara Haban-Beer Stats (17:16):**

Yeah. Look, and I think that just goes to show what the runway is like again. So we go back to one of the things we spoke about earlier and that the penetration rates of ETFs and using ETFs as a vehicle to express your investment view is still relatively low in Australia at the moment, possibly because people don't know what an ETF is, so it's an exchange-traded fund, just to reiterate again. So reminding advisors and their investors and all of the clients that we speak to that ETFs are inaccessible and easy to understand transparent and cost-effective way to access an investment view, whether it's a sector or a geography is obviously a great message to share, and I'm always happy to share that.

Some of the other questions I get are, "Who uses ETFs?" Well, really, that's everyone. So we think there are many different client segments, including the very largest from sovereign wealth funds to large asset owners to active managers, interestingly. So active portfolio managers often use ETFs as well for various reasons, to model portfolio builders, and of course, everyday retail investors like you or I. The use case for ETFs is growing all the time, and they are a terrific liquid, easy-to-access tool for all types of investors. We also get, the questions, I can think of many questions. One of the common questions we get is, "How do ETFs impact stock prices?"

**Jacinta King (18:47):**

Yeah, I did want you to cover that one because that's something that we see in our work as well.

**Tamara Haban-Beer Stats (18:51):**

So in short, the majority of ETF activity doesn't affect the market prices of underlying stocks because the reason for that is most of the activity in ETFs happens on what we call the secondary market where units of the exchange-traded fund are bought and sold between the existing holders of the units and buyers and sellers. It's only when the primary markets, what we call the primary markets are involved. So that means when a ETF unit is created or redeemed, does underlying stock trading need to occur? It's a relatively small proportion of the overall ETF flows. So in Asia Pacific, we've calculated that roughly about 1 1/2, certainly less than 2% of stock trades can be linked back to or attributed to ETF flows.

**Jacinta King (19:46):**

Thanks. I think that, yeah, giving that percentage gives some perspective of where it fits, so thank you. It's a reminder, I think for us in this exchange-traded product space that whether someone is new to investing or a seasoned investor, they may not know the details of exchange-traded products and how they can be considered in an investment portfolio. If our listeners would like to know more about



iShares, please head to their website, [blackrock.com/au](https://blackrock.com/au) and look for individual and iShares. From there, you'll find investor education and insights as well as product information pages. Of course, you can head to the ASX for information on any of iShare's listed funds. Thank you also to our listeners. You can enjoy more of our podcasts, which are released monthly, or sign up to our newsletter investor update by heading to the ASX blog, [buyerasx.com.au/blog](https://buyerasx.com.au/blog). If you look for investor tab on the ASX website, there's a lot of great resources and education sections available there. So thank you for tuning in, and a big thank you to you, Tamara, for joining us today.

**Tamara Haban-Beer Stats (20:45):**

Pleasure, Jacinta.

**Jacinta King (20:46):**

Thanks. Until next time.

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