Three habits of highly effective ETF investors

The evolution of exchange-traded funds (ETFs) has made it possible for retail investors to construct cost-effective investment portfolios that could not have been imagined a decade ago. These financial instruments enable individual investors to achieve diversified exposure across asset classes and geographies while allowing asset managers to quickly create and deploy solutions that accommodate the prevailing 'big picture' trends.

"ETFs are resilient in offering consistent exposure to different macroeconomic themes," says Kingsley Williams, Chief Investment Officer at Satrix, speaking at the recent *IndexMore webinar*, an educational collaboration between Satrix and BlackRock.

The *Global Investing with ETFs: 2021 and Beyond webinar* explored how ETFs - traditionally thought of as index or passive solutions only - were enjoying growing acceptance among active fund managers. BlackRock, one of the largest asset managers globally, says three habits separate highly effective active ETF investors from the crowd, including their ability to understand portfolio construction, identify and combine sources of return, and use the entire investment toolbox that is at their disposal. There is a growing consensus that ETFs can add value to any investment portfolio, whether actively or passively managed.

1. Understanding portfolio construction

One of the features that distinguish ETFs from other financial instruments is the market players' ability to quickly develop and offer an off-the-shelf, risk-adjusted solution that takes advantage of emerging trends or themes. It makes more sense for active managers to purchase a single solution that captures trend returns rather than building a solution in-house, from scratch.

Nothing better illustrates the power and rising popularity of ETFs than the recent push into China. Capital flows into China via ETFs were ten-times higher in 2020 than the preceding year. "The growth in popularity of ETFs can be ascribed to the growing number of use cases for such funds and the greater granularity that can be achieved by using them; they are no longer viewed as tactical vehicles within portfolios but as strategic holdings," says Stephen Cohen, Head of EMEA, BlackRock.

Active asset managers are now using ETFs to achieve risk-appropriate exposure to inaccessible sectors of the market, such as alternative assets and high yielding Chinese government bonds. Against the backdrop of US$17 trillion in global bonds offering negative yield, it is no surprise investors are turning to the Chinese bond market. China is home to 55% of all global bonds that yield over 2.5%.

2. Identifying and combining sources of return

Asset managers are also increasingly turning to ETFs in their search for new ways to generate portfolio returns in a low yield investment environment. BlackRock says that return derives from broad market exposure and strategic factor tilts, with additional return coming from security selection, as well as market and factor timing.

Today's equity returns debate often devolves into whether growth stocks will continue their current trajectory or whether value is coming to the fore. However, stock picking is no longer considered the be-all and end-all of asset management. "We have come from a time when security selection was deemed to be the only driver of portfolio return … nowadays, we have to get exposure to different factors and ensure that we have the tools needed to capture those factors and blend them together," says Cohen.

3. Using the entire investment toolbox

How do you bring together all the instruments that can play a valuable role in your portfolio? "You must make sure that you have the technology that allows you to understand the risks so that when you are investing more in China bonds, using a factor ETF or a high alpha stock picker, you know what the overall net aggregate result of that is on your portfolio," says Cohen.

There is broad consensus that Covid-19 has accelerated global geopolitical transformation. The dynamic between China and the United States is a perfect example, with many wondering why we still think of the US as an investment market while China is considered 'part of the emerging market'. China is growing, fast. It is one of few country markets to emerge from the crisis with positive economic growth. And its stock market looks strong too, with earnings per share (EPS) forecast to grow by 16% in 2021 and by double digits in the following year. "China is starting to emerge as a standalone equity market," says Cohen.

"We are going to see significant changes in indices over the next five years, and that will force investors to rethink what role China plays in their portfolios," he adds.

The EMEA region has experienced a 20% average annual growth in ETF capital over the past five years. The trend is set to accelerate as asset managers realise the potential of equity and fixed income solutions in this market. "We are witnessing a shift towards a more holistic portfolio construction process encompassing fund selection and portfolio risks in a seamless, circular process," concludes Cohen. He notes that active asset managers must understand each fund's real risk characteristics in their portfolios and appreciate how these risks blend together. And this means that a portfolio of best funds is no longer the best portfolio.

Satrix agrees, “The way we build portfolios is changing,” concludes Williams. “We believe that ETFs will serve both active asset managers and retail investors in providing investment solutions that address our triple concerns of low yield, high fees and unintended outcomes.”

ETFs available on the Glacier platform

During 2019 Glacier partnered with Satrix, the leading provider of passive investments in SA, to make a limited range of ETFs available directly on the Glacier platform. ETFs available include:

- Satrix 40 ETF
- Satrix Global Aggregate Bond ETF
- Satrix MSCI China ETF
- Satrix MSCI Emerging ESG Enhanced ETF
- Satrix MSCI Emerging Markets ETF
- Satrix MSCI World Equity ETF
- Satrix MSCI World ESG Enhanced ETF
- Satrix Nasdaq 100 ETF
- Satrix S&P 500 ETF

Investors can combine ETFs with actively managed funds for optimal performance across their overall portfolio.

The ETFs are available as an investment option on most of Glacier’s solutions, including the retirement annuity, preservation fund, Investment-Linked Living Annuity, Investment-Linked Lifetime Income Plan, endowment and Tax-Free Investment Plan.

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