There's more to

STORY MATTHEW GIBBS

A smorgasbord of products, from ETFs to hybrids and warrants, allows investors to diversify their portfolio and manage risk.

When ASX was created in 1987 with the merger of Australia's six State-based exchanges, the 'S' in the acronym stood for 'Stock' – as in the stock or shares of listed companies. The Australian Stock Exchange was the marketplace where company stocks were bought and sold.

But the S needed updating when ASX acquired the Sydney Futures Exchange in 2006. The enlarged exchange required a more encompassing name beyond stocks. S became 'Securities' to better reflect the array of financial instruments now available. The Australian Securities Exchange was born.

In truth, ASX always offered more than stocks and shares. Does Just Jeans only sell jeans? There's value in matching your tops to bottoms at the one place.

Today the S could stand for smorgasbord, after the Swedish word for a table full of different sandwich offerings, such is the variety of ASX's investment delicacies.

While a smorgasbord provides tempting and tasty diversity, you should always know what you're putting in your mouth.

ASX than shares

The bill of fare

"Australian investors love backing businesses they're familiar with. So, there'll always be demand for listed equity," says Andrew Campion, ASX's general manager of investment products and strategy. "But now, in addition to using shares, retail investors can assemble a diversified portfolio made up of different product types and asset classes, and with local and international exposure."

Ian Irvine, who worked at ASX in its investment products team for more than 14 years and now heads the Listed Investment Companies & Trusts Association (LICAT), says it surprises many investors to learn that there are more than 680 investment options or funds with a combined market cap in excess of $480 billion available on ASX beyond single shares in listed companies. These funds include listed investment companies and trusts (LICs and LITs), exchange traded products (mostly exchange traded funds (ETFs)), property funds and infrastructure funds.

But wait, there's more. ASX's investment marketplace also offers Australian government and corporate bonds; equity, interest rate and commodity futures and options derivatives; and hybrids and warrants. It's a veritable feast.

Investing beyond shares can help manage risk and open opportunities for wealth creation. Accessing that variety on ASX with your regular broker provides confidence and convenience.

This view is supported by Rachel Waterhouse, CEO of the Australian Shareholders' Association (ASA). "While focused on equities, many of our members hold other investment products too, such as ETFs, bonds, and LICs and LITs. The variety enables diversification and helps manage risk."

The ASX website (asx.com.au) is rich with information about the risks, benefits, pricing and performance of different products. Here's a taste.

Exchange traded funds

ETFs pool investors' money and invest in underlying assets such as shares, bonds or commodities. When you invest in an ETF you own units in the ETF and the ETF owns the underlying shares or assets. They trade, clear and settle in a similar way to shares. ETFs are open-ended, meaning the number of units on issue can increase or decrease in response to demand and supply. This helps them trade at or near their net asset value.

"ETFs are now more than 25% of holdings for those under 40, which is astonishing, although only 8% for those over 50. For those who've opened a share trading or investing account in the past 12 months, the numbers are even higher. They're hugely popular," says Gemma Dale, director of SMSF and Investor Behaviour at nabtrade.

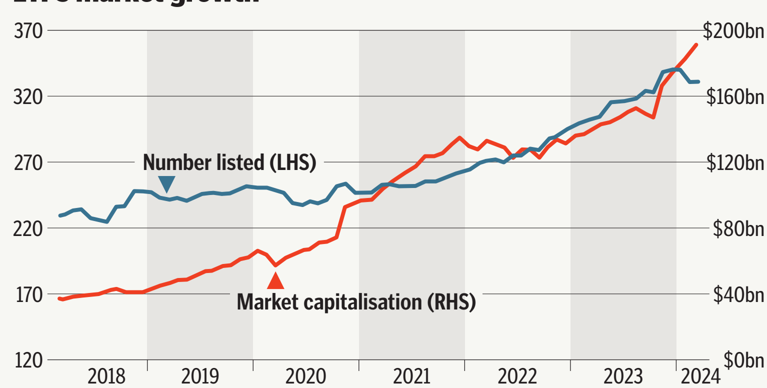
The rise and rise of ETFs is confirmed by ASX's Andrew Campion. While Australian shares remain the most popular of all on-exchange investments, he says total ETF funds under management has grown by $128 billion, from $64 billion in May 2020 to $192 billion as at the end of March 2024.

Among ETFs, Dale says there is strong preference for simple, broad-market index trackers, with several ASX 200 options among the top 10 most popular ETFs. "These are a way to get diversified equities exposure, not a diversifying option for other asset classes."

ETFs with international exposure are also popular, according to ASX data, having the most funds under management – more than $93 billion at the end of March 2024, followed by Australian equities (about $54 billion) and fixed income ($26 billion). Commodities come in at $5 billion.

ETFs are like a buffet in themselves or, as Campion describes, "a wrapper around a basket of securities that trade on exchange and allow investors to build a well-diversified portfolio". ▶

ETPs market growth



Source: ASX ETPs = Exchange Traded Products (mainly ETFs)

Nabtrade's Dale praises ETFs for "removing the biggest barrier for people thinking about investing for the first time – what do I invest in? A lot of investors worry about losing money or making a bad decision or feel unable to research individual companies. An index-based ETF removes that worry. People start investing earlier and build their confidence and knowledge over time. ETFs give people a low-cost, low-effort entry point, which is really positive."

Listed investment companies and listed investment trusts

LICs and LITs provide exposure to underlying securities, often domestic or international shares, and increasingly other asset classes, such as fixed income. Investors' cash is pooled in a managed fund and a professional investment manager selects the fund's securities and invests the cash. LICs and LITs are close-ended, which means the number of shares or units is generally fixed. However, capital can be raised from and/or returned to investors consistent with an entity's active capital management strategy.

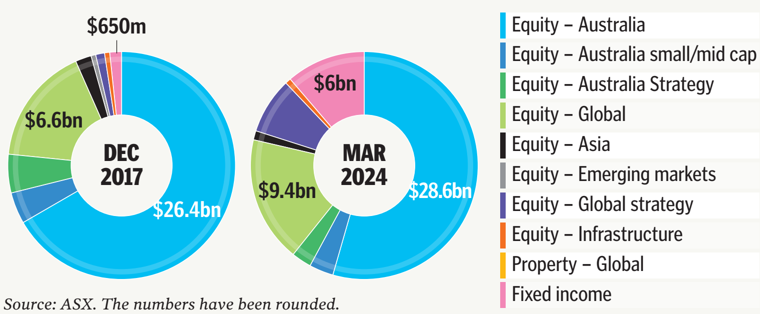
Ian Irvine, who has headed LICAT since leaving ASX in 2017, says the closed-end structure allows for better capital management by active managers on behalf of their investors. "Open-ended structures, like ETFs, can see capital flow in and out, which may prohibit the implementation of long-term investment strategies and add to costs."

Because of their company structure, LICs can generate franking credits and retain profits on balance sheet to pay dividends in future periods, providing a steady income stream.

The $52 billion LIC and LIT sector has a long history. Whitefield Industrials, for example, celebrated its centenary last year. Other well-known LICs include the $9 billion Australian Foundation Investment Company (AFIC).

Nabtrade's Dale says that many of its older and more experienced investors hold LICs rather than ETFs. AFIC and Argo Investments, a $6.6 billion LIC founded in 1946, are in its top 20 holdings.

Shift in split by asset class within LICs and LITs



Source: ASX. The numbers have been rounded.

Bonds

"Bonds are back", according to ASX's Campion, and are "more attractive due to heightened interest rate regimes around the world".

Bonds are a type of debt security, sometimes called a fixed-income security because many pay a fixed rate of interest. They are an IOU between a borrower (the issuer of the bond, such as a government or corporation, which seeks to raise money) and a lender (the investor who purchases the bond). Investors receive interest or coupon payments at certain intervals, and have their principal returned at a future date.

ASX offers exchange-traded Treasury Bonds (eTBs), Treasury Index Bonds (eTIBs), where the capital value of the investment is adjusted by reference to movement in the consumer price index, and corporate bonds, with a fixed or floating rate of interest paid.

There are more than 40 bonds listed, with a market capitalisation at the end of March 2024 of more than $1.6 billion, a rise of more than 48% in 12 months.

Treasury bonds are traditionally beyond the reach of retail investors. ASX makes them accessible. Bonds can potentially provide greater security (especially if the issuer is the Australian government), regular and predictable income and improved portfolio diversity, and help manage the risk of exposure to high-growth assets such as shares. There are potential risks, too, including changing interest rates (if the coupon rate is fixed) and the credit quality of the issuer. ASX has dedicated market makers to ensure liquidity and a fair price.

Typically, Campion says bonds are "a shock absorber or stabiliser, providing a balance to the movement of equities and helping reduce overall volatility in your portfolio".

Nabtrade's Dale says, "If rates continue to stay high and equities have a period in the wilderness, there will be greater appetite for fixed-income products. This will require education, to ensure investors understand the nuances and risks."

Exchange traded options

Exchange traded options (ETOs) are derivatives, such as futures and warrants, that derive their value from an underlying instrument, such as shares, indices, fixed-interest securities and commodities.

They are contracts between two parties that give the buyer the right – but not an obligation – to buy or sell an underlying security at a set price at a specified time in the future. ASX offers ETOs over single securities or an index.

ETOs provide price certainty by 'locking in' a future buy or sell price for a security. This also 'buys' time to make up your mind. They can provide leveraged exposure to the sharemarket, protect your shares from a fall and generate income, and be used in both rising and falling markets.

There are risks and complexities to understand, too, including puts, calls and margins. ASX offers a range of ETO guides and tools, including online courses, webinars, and a new Options Trading Game suitable for all levels of experience.

The ASX investment marketplace also stocks Australian Real Estate Investment Trusts (A-REITs), which provide exposure to property assets such as office towers, shopping malls, hotels and industrial buildings in Australia and overseas; and hybrid securities, which combine elements of debt and equity securities and include convertibles, preference shares and capital notes.

Education is vital

While all these products can play a role in a well-diversified investment portfolio, not everything will be to your taste. As the ASA's Waterhouse cautions, "understand your investment needs" and always "check what's under the hood" of any financial product.

As ever, education and information are vital. Standard, simplified access doesn't standardise or simplify the risk-reward characteristics of products.

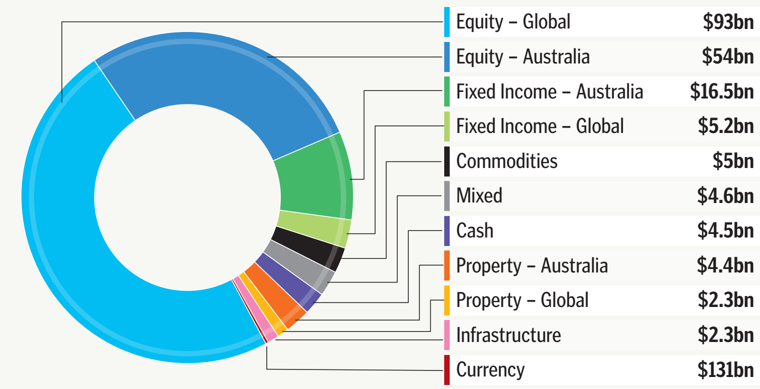
"The market is constantly changing," says Campion, "and there's a regular inflow of new investors with different needs. ASX supports investors through a wide range of education initiatives, including investor days, newsletters, CEO Connect events, podcasts and courses. It wasn't long ago that people thought an ETF was a transfer you did at the supermarket. From new products such as crypto to older ones such as bonds, education is critical."

This is a truth universally acknowledged.

Whether a smorgasbord of sandwiches or securities, consumption rules apply. Eat healthily. Understand the ingredients. Be adventurous and try new things but taste-test first. Don't pig out.

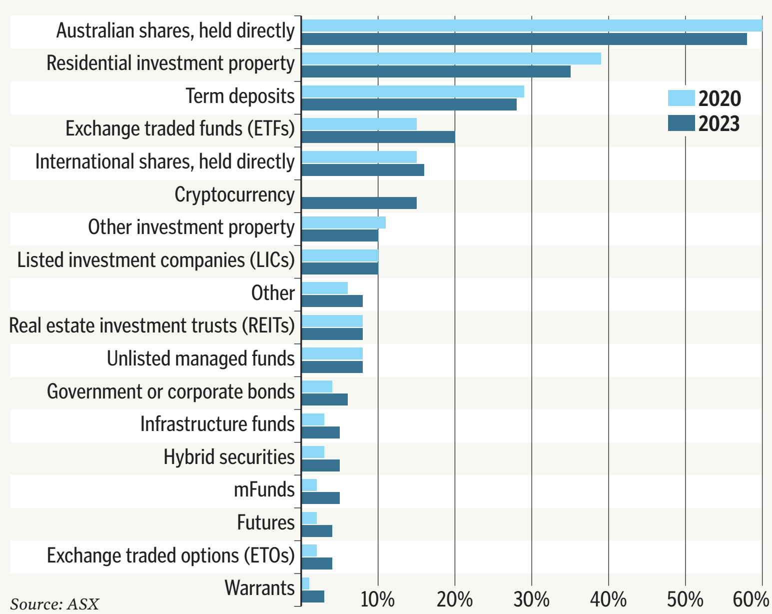
Variety can be the spice of life, and of investing. ■

Asset spread of ETPs, funds under management



Source: ASX, March 2024. The numbers have been rounded. ETPs = Exchange Traded Products (mainly ETFs)

What investors own outside home and superannuation



Source: ASX