



**BetaShares**  
Exchange Traded Funds

# **BETASHARES GLOBAL ETF REVIEW**

**QUARTER 3 - 2019**

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# BETASHARES GLOBAL ETF REVIEW Q3 2019: BURSTING THE BURRY BUBBLE!

## SUMMARY

We're pleased to share BetaShares' Global ETF Review for the third quarter of 2019. This quarter's data highlights the continuation of investors' preference for passive, with passive funds receiving ~US\$87B v. ~US\$20B for active funds in the US. Indeed, this quarter marked a significant milestone with assets in passive managed funds and index ETFs topping those in active managed funds for the first time. That notwithstanding, actively managed funds bucked their current 2019 trend by ending the quarter with positive flows for the first time this year, although they are still in the red over the year to date.

Overall, the global ETF industry ended Q3 of 2019 at a record high of assets under management of US\$5.8T with very fast growth of some 20% YTD.

In a continuation of the yearly theme, fixed income continued to receive the highest amount of flows, although the quarter saw a significant amount of interest and buying into gold/commodity products as investors sought out safe havens from increased geopolitical risk.

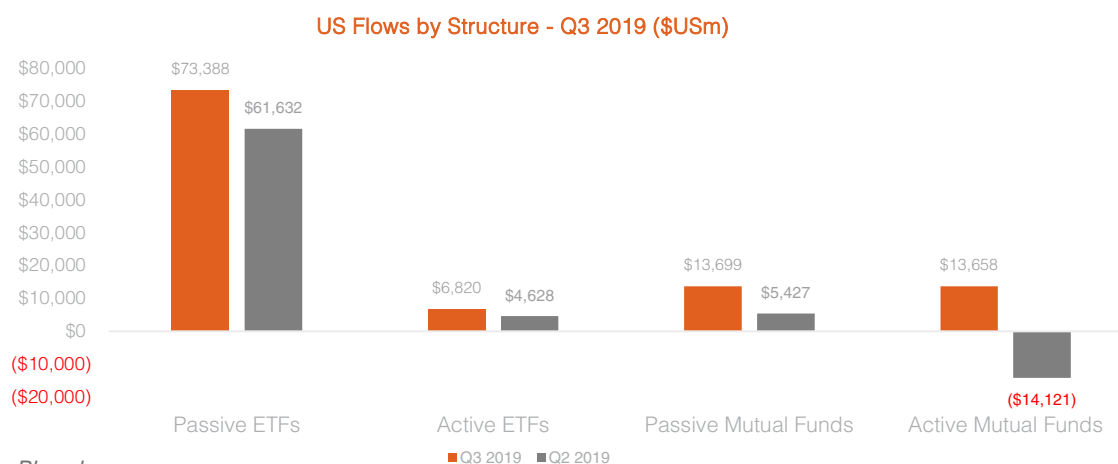
Within equities, it was once again North American exposures that took in the most flows with their share of flows growing substantially. At a sector level we saw Energy and Financials sector exposures sold off as impeachment jitters lingered, along with significant inflows into real estate ETFs which continue to perform strongly.

In this quarter's spotlight, we use data to refute the myth that the growth of ETFs are causing market bubbles or distortions, a topic which has once again come to the fore after a recent article from Michael Burry, a well-known name thanks to the movie blockbuster *The Big Short*.

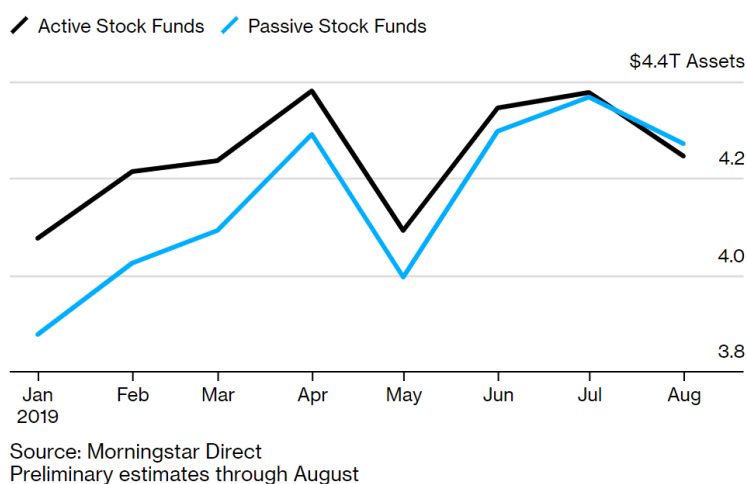
*The BetaShares Global ETF Review* is a quarterly publication which examines the key trends and developments in the global ETF industry. The Global ETF Review has been designed as an accompaniment to our monthly *Australian ETF Review* which focuses on our local ETF market. Given its maturity and scale, our focus in this report is primarily the U.S. ETF industry – which, being by far the largest ETF industry globally, provides interesting insight into trends in markets and investor behaviour. All figures in the report are in U.S. dollars, unless otherwise noted.

## SECTION ONE: ACTIVE VS PASSIVE

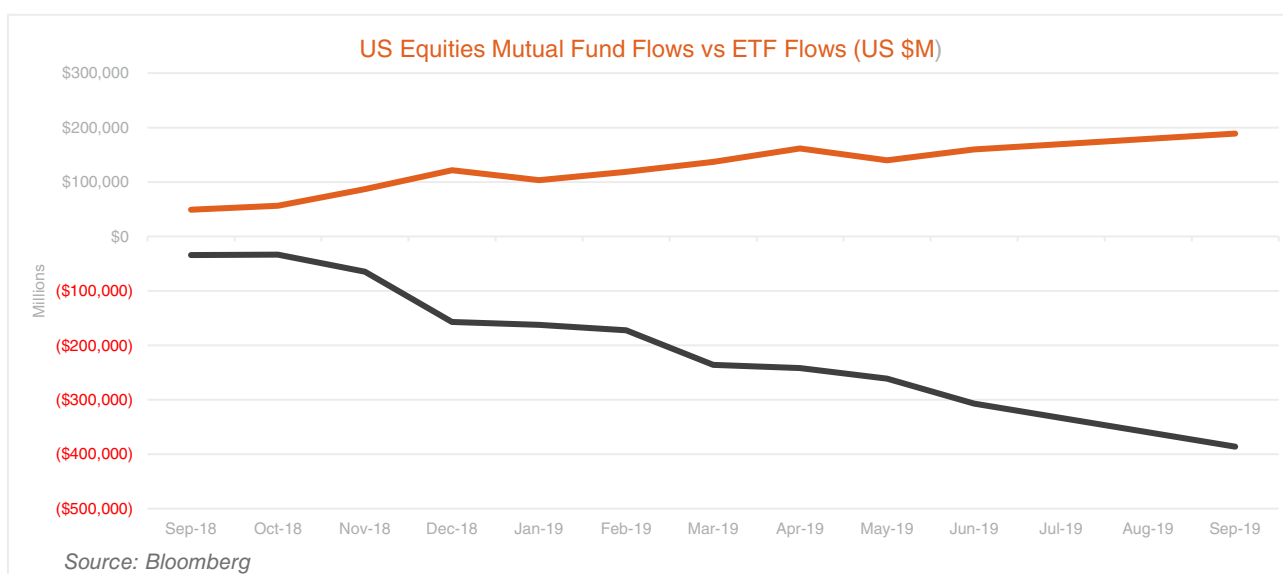
### 1. Flows into Active vs Passive Funds: Q3 2019




- Net flows across investment products in the U.S. lifted 40% from the previous quarter and for the first time in 2019, inflows were positive across **all** product structures – whether ETFs or traditional mutual funds.
- Of particular note this quarter, were the **positive inflows** to active mutual funds which **attracted** US\$13.B, after **6 months of consecutive outflows** during 2019.
- In saying that, however, the positive trend toward ETFs continued unabated, with ETFs capturing **75% of flows in the US investment management industry** in the quarter. **Passive ETFs** in particular lead the way, receiving ~US\$73B of flows– with investors continuing to preference passive v active and ETFs v managed funds.
- Indeed, in a well-publicised statistic, a significant milestone occurred in the US this quarter with assets in passive managed funds and index ETFs topping those in active managed funds for the first time in August, as per the chart below from Morningstar:



## 2. Equity Mutual Fund flows vs ETF flows: 12 Months to 30 September 2019

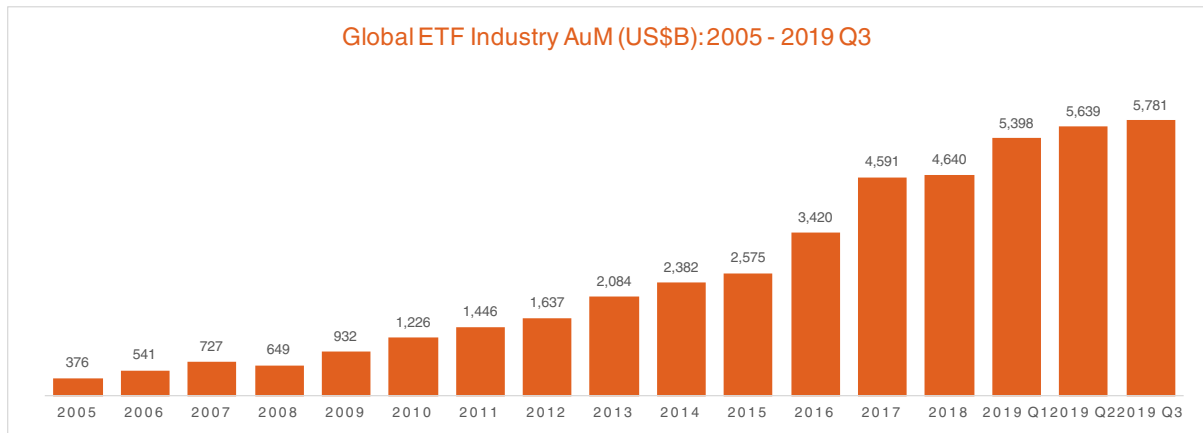


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- Over the last 12 months, **equity mutual fund outflows in the U.S. were US \$386B**, which compared to positive **inflows of \$188.9B into equity ETFs**.
  - This trend appears to be consistent with the experience here in Australia, with Morningstar data indicating that retail managed funds in the first 6 months to June 2019 experienced **outflows of ~\$4B** vs **inflows into Australian ETFs of ~\$4.4B** according to our Half Yearly review.



## SECTION TWO: GLOBAL ETF INDUSTRY

### 2. Global ETF Industry market size: 2005 – Q3 2019



Source: ETFGI. Includes all exchange traded products.

- The global ETF industry ended Q3 with assets under management of US \$5.78T. This represents **an all time high** in terms of assets under management with growth of 2.5% QoQ – and **25% YTD** growth compared to the end of 2018.

#### Trading volumes and ETF numbers

- Other than the obviously striking statistics on asset growth and flows which are presented above, investors are often surprised to learn of the significant number of ETFs around the world (**there were 7,797 ETF/ETPs as at end September 2019!**) and the highly significant trading volumes currently being experienced.
- The chart below is a list of the Top 10 most traded securities on U.S. stock exchanges and trading volumes at the end of Q3. The chart illustrates that, on U.S. stock exchanges, **ETFs were 4 of the top 10 most traded securities in 2018!**
- In addition, and notably, the most traded security of all is an ETF which traded **~3x the value of the most traded company**, Amazon.

Top 10 most traded securities in the US	Trading Values (YTD to Q3 2019, US\$B)
S&P 500 ETF Trust	\$3,966
Amazon.com Inc	\$1,396
QQQ ETF	\$1,125
Apple Inc	\$1,029
Russell 2000 ETF	\$596
Microsoft Corp	\$595
Facebook Inc	\$567
MSCI Emerging Markets ETF	\$530
Alibaba Group Holding Ltd	\$513
Netflix Inc	\$507

Source: Bloomberg

## SECTION THREE: ETF FLOWS – WHAT’S TRENDING, WHAT’S FADING?

In this section of the Review we look at the flows in the global ETF industry by category. Given the sheer size of the U.S. ETF market, analysis of these flows is useful to generate insight into investor sentiment and behaviours, although other markets are examined.

### U.S. ETF flows by asset class: Q3 2019

Equity Fund Flows by Asset Class (\$US m)	2019-Q3	%	2019-Q2	%
Fixed Income	\$37,818	48.4%	\$39,388	61.2%
Equity	\$29,488	37.8%	\$24,371	37.8%
Other (see break down below)	\$10,766	13.8%	\$638	1.0%

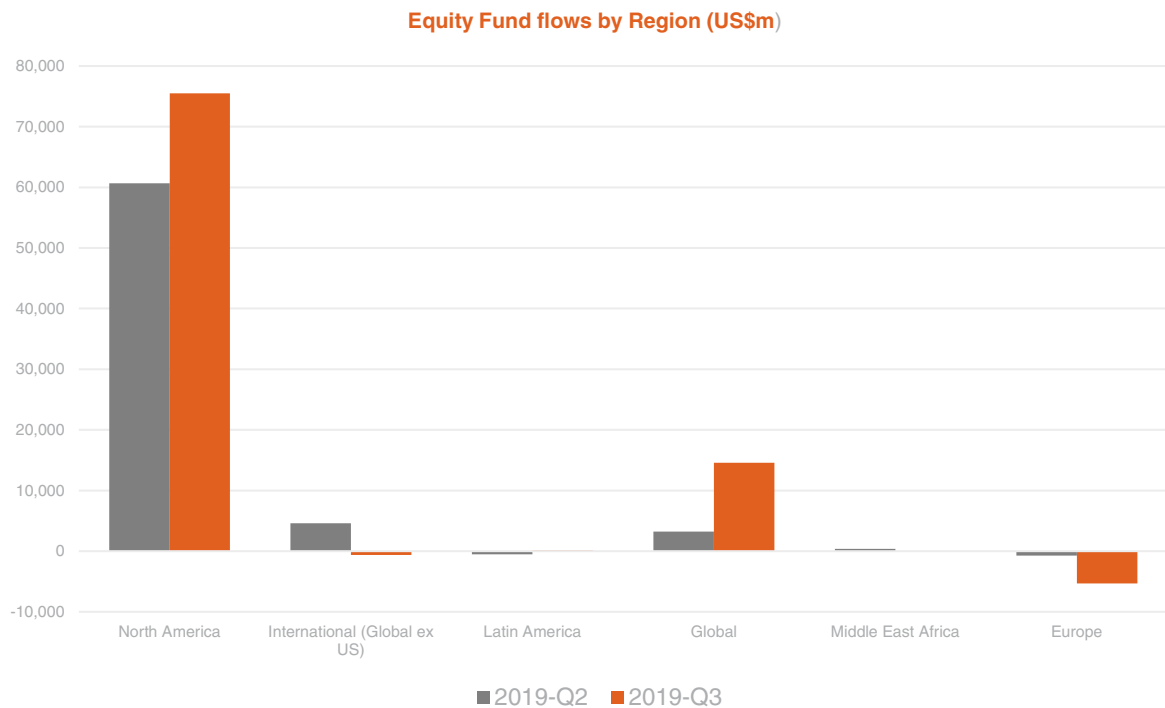
Equity Fund Flows by Other Asset Class – subcategory breakdown (\$US m)	2019-Q3	%	2019-Q2	%
<b>Commodity</b>	<b>\$9,236</b>	<b>10.4%</b>	<b>\$174</b>	<b>0.3%</b>
Specialty	\$1,129	1.3%	\$294	0.5%
Mixed Allocation	\$512	0.6%	\$337	0.5%
Money Markets	\$3	0.0%	(\$2)	0.0%
Alternative	(\$112)	-0.1%	(\$165)	-0.3%

Source: Bloomberg

- In a continuing theme for the year, it was the Fixed income category which received the highest flows this quarter, albeit this quarter’s flows were a lot more balanced than the quarter before. Fixed Income as a category received ~48% of flows which was **13% less flows** than the previous quarter, with investors turning their attention to commodities exposures, which attracted 10.4% of category flows vs 0.3% the previous month.
- Most of commodity inflows came from gold and silver, with strong demand for precious metals as investors sought out safe havens due to increased geopolitical risk. Gold itself surged briefly after a drone strike on the Saudi Arabia’s Oil production. The price of gold gained 5.42% for the quarter
- As is often the case, the theme of flows was mirrored here in Australia, with **fixed income** being the highest category for inflows as at September, receiving ~\$2.5B of net flow, we have also seen meaningful flows into gold products here in Australia, with approximately \$300m of net flows over this period.

### 3. Share of U.S. Equity ETF fund flows by:

#### a. Region – Quarterly

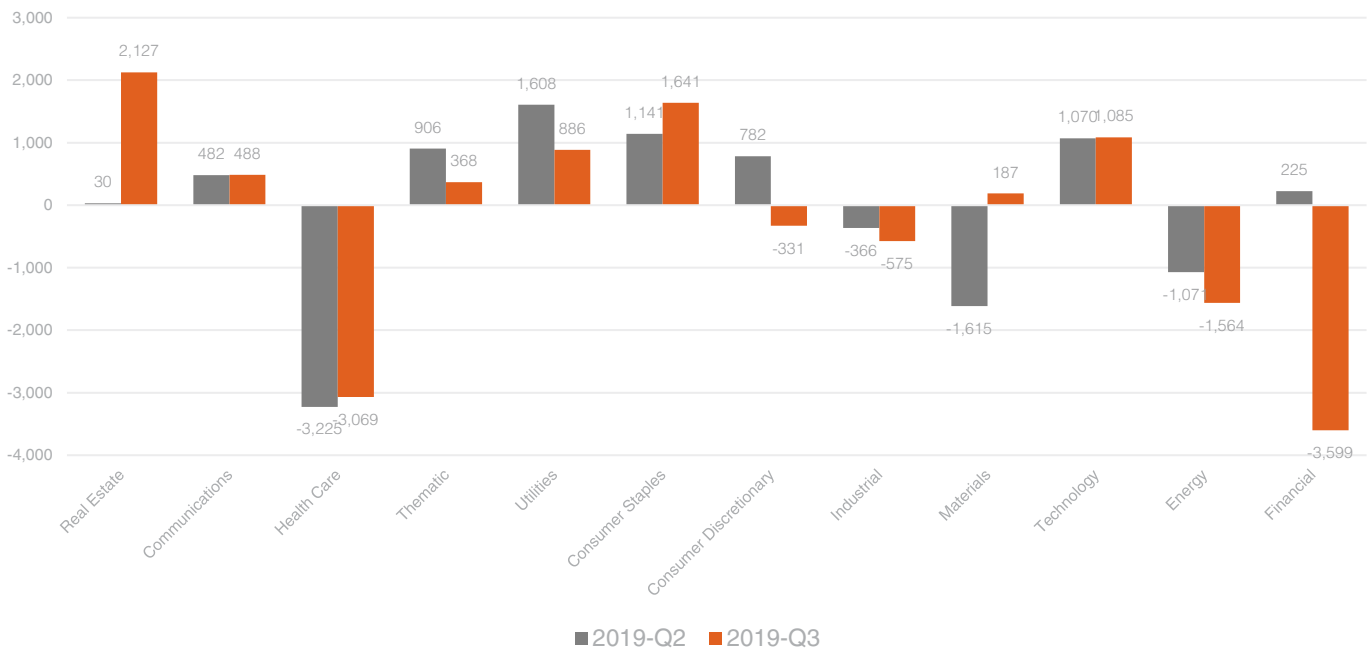


Source: Bloomberg

- Much like Q2 of 2019, North American exposures continued to dominate with ~95% of flows
- Global products, however was the Q3 “comeback king”, attracting ~18% of flows during the quarter – an over three-fold increase from its Q2 level of 5.1%
- Europe and Asia continued their 2019 trend, experiencing another quarter of outflows reflective of trade tensions and Brexit uncertainty.

## b. Sector – Quarterly

Equity Fund flows by Sector (US\$m)



Source: Bloomberg

- Cumulative flows for sector ETFs ended up in the red during Q3, with ~US\$245m in outflows as rotation towards fixed income and commodities continued.
- In particular, Energy and Financials sectors saw large outflows as impeachment jitters lingered. Healthcare, as was the case last year continued to fall out of favour with investors with outflows US\$3.0B.
- That said, we saw a large reversal of fortunes for a number of sectors, including Real Estate which had US\$2.1B of flows after a very flat second quarter.
- Consumer Staples which includes ‘everyday’ products such as food, beverages and household goods saw **positive inflows of US\$1.6B**. Furthermore, due to the non-cyclical demand of consumer staples, it’s **one of only three sectors to have attracted consistent positive flows during 2019**.



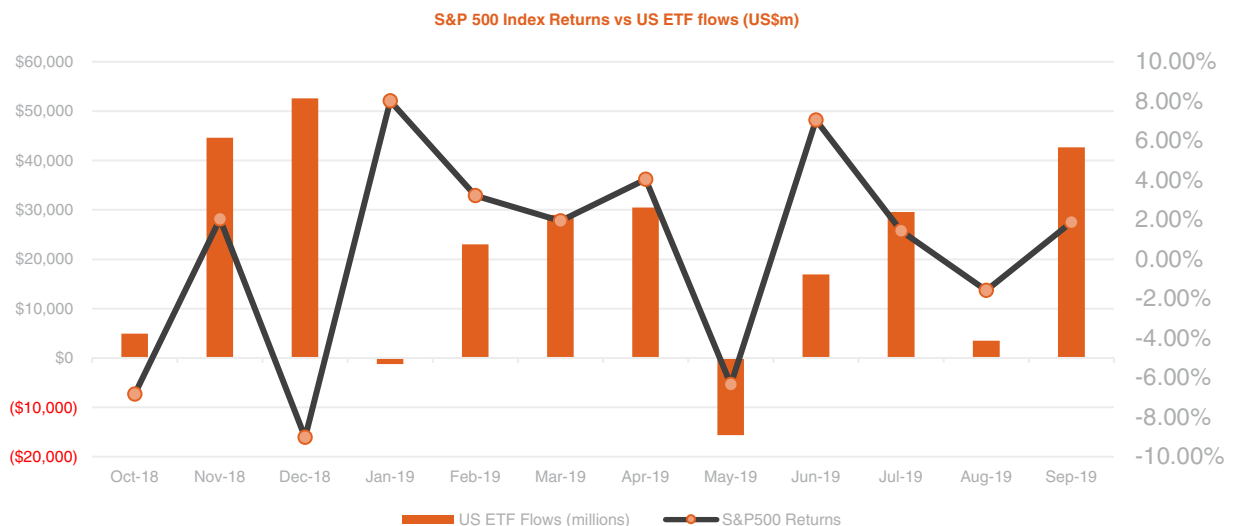
## SECTION FOUR: SPOTLIGHT

In this quarter's spotlight, we're focusing on "an old favourite" - namely the theory (fable?) that the growth of ETFs is causing market distortions or 'bubbles'. This topic pops up from time to time, but has come back into vogue recently after a recent article from Michael Burry, a hedge-fund manager who rose in popularity thanks to the financially themed-movie *The Big Short* (Michael is the character played by Christian Bale, who famously 'called' the US housing bubble which ultimately led to the global financial crisis).

One piece of advice that the humble author of this report lives by is to try to understand the motivations of someone who puts out sensational 'news-bites' to make sure they are 'pure' and not 'loaded' and, in addition, as a way to determine argumentative strength to check whether said 'news-bites' is backed by empirical evidence or mere conjecture. It appears that, for Michael, the answer in this case is: a) his motivation, and the motivation of many of theorists who have put out this theory before him is to demonise and perhaps destabilise the growth of the disruptive investment product that threatens his commercial existence - ETFs and; b) that Michael has not backed up his argument with any solid evidence.

As a counter-argument, I thought I would let the figures do the talking! Before doing so, it's important to note that an ETF is nothing more than an investment wrapper (albeit a very effective one!), which houses investment exposures which in turn are used by investors to express investment views. It is these views, and the buying or selling of the exposures themselves, not the wrappers they are contained in, that cause markets to rise and fall. In other words, investors move markets and will find ways of doing so, whether individual stocks, managed funds or ETFs!

### 4. Spotlight: Bubbles & Burry

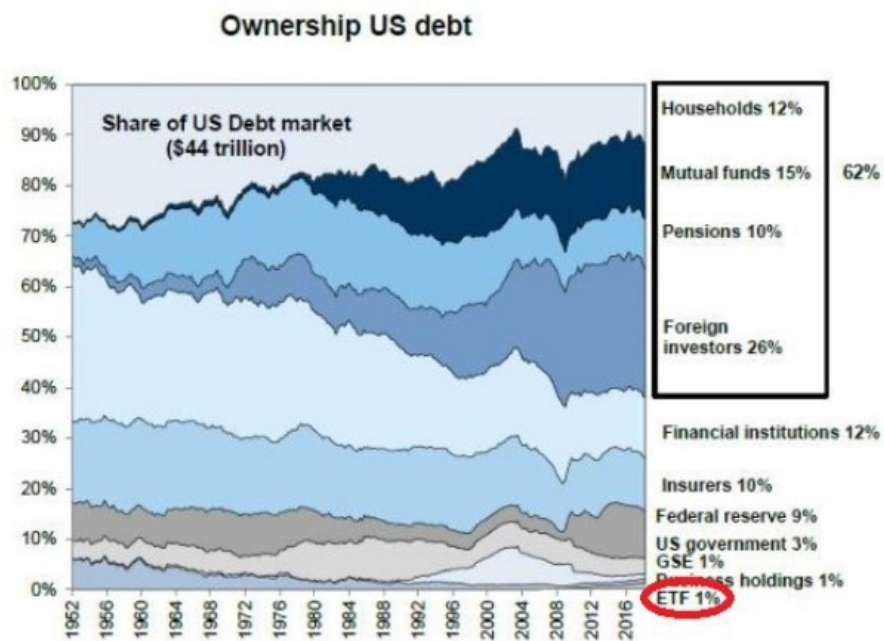
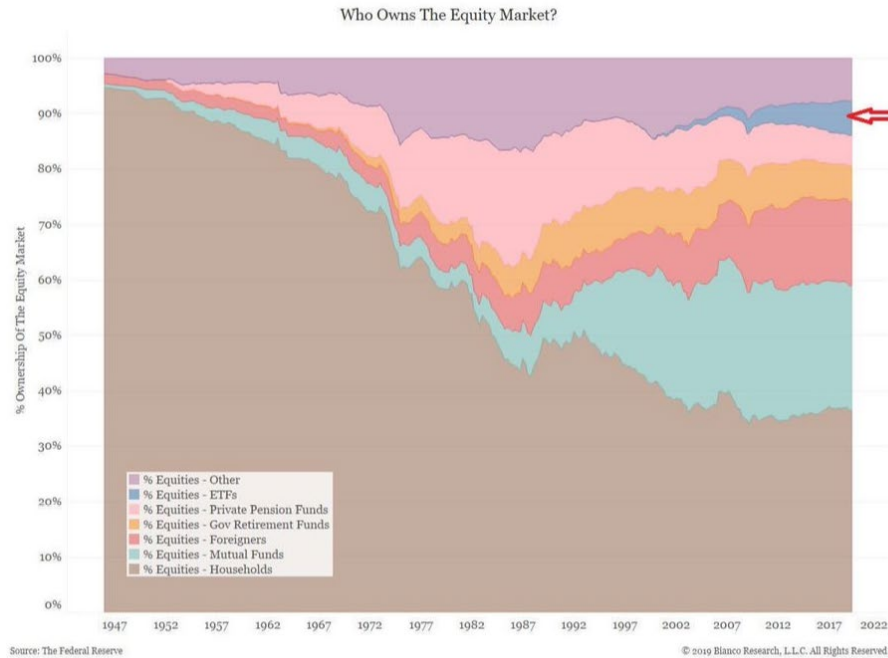


Source: Bloomberg

- To me, in many ways, to refute Michael's argument, the above chart is all one needs. It shows the recent flows in US equities ETFs plotted against the returns of the benchmark S&P 500 Index.
- As can be clearly shown, there is an **independent relationship between ETF flows and market pricing**. See for example December 2018! A great chart to use if anyone asks such a question in the future!

- Notwithstanding the above there may be some who continue to push the 'price distortion' argument. This claim can be easily refuted by reference to the relatively small market share that ETFs own of underlying securities – clearly illustrated in the charts from the Federal Reserve (on equities) and Goldman Sachs (on debt) below.

You see Michael, we're doing really well, but we're still small bikkies in the scheme of things!





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