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Market Update

Investors brace for another bout of market volatility as US-China relations take a turn for the worse, with a brewing tech cold war now on the agenda. Equity markets lost steam over May breaking the start of 2019's four-month rally. Though, on a total return basis, the US S&P 500 was down -5.1%, the ASX 200 defied global momentum, rising 1.7% mostly supported by rising iron ore prices, and the Coalition's election win.

In latest US-China developments, President Trump has blacklisted Chinese tech firms deemed a national security threat, restricting the likes of Huawei and ZTE from doing business with American companies, following a breakdown of trade negotiations and a subsequent increase in tariffs. The move has aggravated China who has since signalled little interest in resuming talks with the US while retaliating with threats of their own.

The International Monetary Fund (IMF) has warned that the US-China trade war has already caused substantial damage, and that a failure to resolve differences alongside further escalation in other areas could dent business and financial market sentiment.

While the US Fed's patient approach towards monetary policy is believed to be appropriate for now, the Fed will be watching incoming economic and financial data closely to assess the case for a shift in monetary policy direction. A cut to interest rates could become a more attractive option if inflation continues to disappoint with annual core PCE, the Fed's preferred measure of inflation, having been reported to hold at 1.6%, below the Fed's 2% target.

Of some relief, the Eurozone economy was reported to have expanded by 0.4% in the March quarter. The past month's data has been positive, with the final reading for core consumer price inflation in April recording the firmest pace since mid-2015 at 1.3% year-on-year. Meanwhile, Italian political tensions heighten as the country's Deputy Prime Minister grows increasingly prepared to breach EU Budgetary guidance. On Brexit, the path remains clouded with uncertainty as Prime Minister May announced her resignation, following an attempt to push her many-times amended Brexit deal through parliament for a fourth time.

Domestically, the Reserve Bank has left the cash rate unchanged at 1.50%, but with unemployment having inched up to 5.2%, despite ongoing jobs growth, consensus is favoring up to 3 cuts in the cash rate over the next few months. In other news, the Coalition retained government having won the Australian Federal Election, against all expectations of a swing in support to the Labor Party. The Morrison Government's victory served as a relief to the markets with the threat of Labor's policies targeting franking credit refunds and changes to negative gearing off the agenda.

Sustainable investing

There is no doubt that interest in responsible investments is growing.

Not only in Australia but globally, investors are increasingly interested in how a company makes its money, not simply how much it makes. While some investors may focus on the longer-term viability of a company and its behaviour, others may hold particular values they want their investments to mirror. How these two strategies play out in the investments context can be different. We explore the rise of sustainable investing in more detail.

Changing investors' perception.

Even at the highest level, investors are shifting from only looking at short-term returns to a broader focus on long-term value creation, including the impact a company is having on those around them. In his 2017 letter to the CEOs of the companies his firm invests in – Blackrock CEO, Larry Fink, highlighted this exact issue noting that "To prosper over time, every company must not only deliver financial performance, but also show how it makes a positive contribution to society. Companies must benefit all of their stakeholders, including shareholders, employees, customers, and the communities in which they operate".1

More and more investors are asking CEOs to focus not only on creating shareholder value, but also on long-term vision for the company, and, by extension, the impact it will have on society via investing sustainably.

It's not a new idea

Today, many investment managers, including BT, use environmental, social and corporate governance (known collectively as ESG) knowledge and data. It can help to inform the analysis of important areas including risk and innovation to engagement and voting practices.

Examples may include a company's interaction with the environment, such as water and air pollution, social factors like employee diversity or safety standards, along with the company's governance structure, such as how the board is composed and compensation structures. This approach seeks to add value or manage risks through broader, more comprehensive investment analysis, decision-making and engagement with companies.

Investing opportunities

For investors, navigating the world of responsible investment can be complex. Terms like ethical, sustainable and impact investing are often used interchangeably by investors seeking to ensure that their money is invested in companies or funds that mirror their values and beliefs. In reality, these terms each relate to a specific type of responsible investing – depending on what the investment is trying to achieve.

Ethical investing verses sustainable investing

Arguably, the most well-known responsible investment strategy among investors is ethical investing. This strategy's primary purpose is to exclude certain industry sectors, companies, practices or even countries that meet specific criteria from a fund or portfolio, based largely on the client's preference not to be invested in these activities. Traditional ethical investment strategies seek to avoid issues like tobacco, weapons, gambling, and pornography; however, investors are increasingly interested in strategies that avoid sectors linked to climate change or abuse of human rights.

1. https://www.blackrock.com/corporate/investorrelations/2017-larry-fink-ceo-letter

Sustainable investing, in contrast, is a type of responsible investing that considers ESG issues in an investment, alongside standard financial measures when assessing a company's performance. This might include how a company approaches employee relations, executive remuneration and anti-money laundering legislation.

Sustainable investing also lends itself to longer-term investment horizons and strategies. If more investors use a sustainable strategy in their investment decision-making, more and more companies will be encouraged to behave sustainably and address ESG concerns and opportunities in their business.

Impact investing is a rapidly developing field

You may also have heard about the rapidly developing field of impact investing. Impact investments preference the social or environmental purpose of an investment over or alongside its financial results. Whilst there are currently few opportunities to access impact investments for most retail investors, many people are attracted to the idea of investments that aim to deliver a positive outcome as an alternative or complement to traditional philanthropic funding.

It's kid stuff: we need to talk about money at home.

Pocket money is a good start but there's more to teaching kids about finance.

Parents spend years preparing their children for the world but, with so much knowledge to pass on, teaching good money habits may take a back seat.

Yet teaching kids how to build wealth, manage debt and avoid financial pitfalls is one of the best gifts you can give them. And the task has taken on a new global urgency.

Policymakers around the world are now working on improving our low levels of financial literacy, which is seen as one of the contributing factors to the global financial crisis1. Governments are introducing programs to educate both young and old on better ways to manage money, provide for their retirement and negotiate the increasingly complex financial products and services available.

In Australia, educating the next generation is one of the main goals of the National Financial Literacy Strategy2.

The strategy, led by the Australian Securities and Investments Commission (ASIC), promotes the value of teaching financial literacy in schools. But it's not just about formal education. Parents, families and peers also have a big role in shaping young people's approach to money.

Our money habits are largely formed by the time we are seven years old, according to UK research3, so parents have an important role in influencing their children's financial future.

Everyday family life presents many opportunities to talk to children about money, involve them in budgeting and planning and learn valuable skills, says ASIC4.

Sadly though, ASIC's research shows that only around one in six families discuss household finances with their children5.

Nonetheless, primary school students have a good knowledge of earning money, a national study has found, although they're less competent at budgeting. The study, published in the CommBank Common Cents Report6, found:

- 68% of children liked saving their money more than spending it
- 77% understand that they can earn extra money by doing chores around the house.
- 50% know what a budget is
- 69% receive pocket money and 82% are expected to complete tasks to earn it

Given the choice of taking $5 now or waiting longer for a larger amount, more than half of the children surveyed said they'd rather take the $5 immediately.

To develop the report, CommBank determined five core competencies that make up a strong financial acumen: spending, saving, earning, budgeting and investing. You can test your child's financial literacy here.

As technology increasingly plays a part in financial transactions, meaning that cash is often not used, children need help to interpret what they see around them and to alert them to risks.

For example, children watch their parents hand over a plastic card at the supermarket to pay and then often receive cash back, says mother of two Nicole Jamieson*.

There's also the often bewildering array of mobile phone plans to come to terms with. For a tool (or toy) that's now owned by many children, understanding the benefits and risks of mobile phone plans is a crucial skill.

A part-time job is a great teacher

While younger children may struggle with the concepts of earning and saving, despite a system of pocket money, their first job can bring the lightbulb moment.

Jamieson, whose daughters are now 17 and 21, struggled through the pocket money years. "It's fraught because you want them to earn money but you feel you shouldn't pay them to do all the chores."

When the children were in their early teens, Jamieson and her husband believed that pocket money was to cover any discretionary spending.

"But the challenge here was that things cost so much more now and if, say, kids go to the movies, it's quite expensive. So the difficulty was in expecting them to pay for all their discretionary spending."

Now that the girls are older, with one at university and the other in her last year at school, both have part-time jobs and they've rapidly become more financially literate.

"Parents can talk on and on about money but it all clicks into place when kids experience earning and saving in the real world," says Jamieson.

"Our younger daughter has had a job for a year and a half now and she's saving up for her gap year. She's quickly learned all the things we'd hoped she'd learn, which is how hard money is to earn and how it is easy to spend. Working has really cemented her understanding of money." Nonetheless Jamieson finds her daughters and their friends are worried about their financial futures. "They hear murmurs from older relatives that buying a house is never going to happen and then there's the job market – some kids are quite anxious about it," she says.

"So it's a tough time for kids and we want to build their skills without giving them more anxiety than they might pick up. But we hold to the old principles spend less than you earn and certainly a part-time job teaches more than you can ever say."

5 tips for teaching kids about money

ASIC's MoneySmart7 has some ideas for parents:

- At the ATM, explain where the money's from and how you've earned it.
- For groceries or other household purchases, prepare a list, research prices and discuss how you can save money if you shop around.
- Involve the kids in discussions about family budgeting can help them learn to differentiate between needs and wants, costs and spending.

- Pocket money or income from a part-time job present opportunity to discuss setting financial goals and saving.
- Discuss options for mobile phone plans and the need to check and manage data usage to control costs.

For more advice on how best to teach your kids about saving for their future, talk to your financial adviser.

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