Stoxx readies third generation of customised indices for structured products

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Pablo Conde

In the second part of an interview, Matteo Andreetto (*pictured*), chief executive at Stoxx, provides an overview of the firm's Select Diversification Solutions (SDS) range for structured products and how market developments are pushing the index provider to continue to innovate and expand its offering.

"We, at Stoxx, don't like to sit around and wait for what is coming next, and we have already been working on how to expand the SDS range," says Andreetto.

The first generation, says Andreetto, was about evolving the benchmark with low correlation, low volatility and high dividend strategies to create a cheaper option and an attractive upside for investors; the second generation was about optimising the benchmark with the minimum risk and the maximum dividend using correlation instead of filtering to lead to an even cheaper option and more attractive structures.

"The idea behind the third generation which we are developing currently is basically using the optimiser to get the minimum option price," says Andreetto. "With the third generation we are effectively entering the brickworks and instead of optimising the volatility of an index we are optimising the gamma, and that requires an additional investment in technology on our side because we need to implement single and multi-asset optimisers, and a 'pricer' built into the index construction."

According to Andreetto, the aim with the third generation is to provide a set of underlyings to build more attractive structured products by looking at the volatility structure and the risk-reward of the indices.

"This will allow us to create differentiated themes by having a multiple dataset managed as an open architecture, and leverage that in the context of providing solutions which price cheaper and therefore result in potential better returns for the end investor," says Andreetto.

Stoxx's market share, says Andreetto, suggests that the firm continues to set standards in the market. "But we also want to be innovators in the derivatives space and to achieve that you have to strive for perfection and be ambitious when you set your goals," he says. "Setting standards is not only about the technology you use to create your offering but also about your ability to identify market trends, providing tools to clients, and facilitating an entire ecosystem for product manufacturers and investors."

Stoxx publishes a **quality charter** relating to decrement indices for structured products on its website to provide extra transparency and information to issuers.

"We want to show that the underlyings we provide are based on high quality standards but also aim at delivering performance," says Andreetto. "We are also in regular contact with the regulators to ensure that all the concepts we work with are within the existing requirements and are also suitable for retail distribution."

This, according to Andreetto, is also a differentiating factor for Stoxx as a provider of indices for financial products as well as the fact that Stoxx index review decisions are not committee based.

"We want to provide strategies that are not subjective in any level," says Andreetto. "Being part of the Deutsche Börse Group also adds scope to any concept we develop as it can potentially become a listed derivative."

The SDS range, says Andreetto, is open to any kind of strategy and index designed and developed by Stoxx. "That's the power of the technology we have developed," he says. "The way the SDS range has been developed also mirrors market trends and investment themes."

The second generation (the whole Stoxx Select and Diversification Select families) shows a move towards the optimisation of structured products focusing on the low carbon concept, ESG/SRI and global baskets of indices. The theme-based and also global basket indices are the extension of these families which use the same SDS overlay.

"We call them "hybrid index concepts" as they combine not only the low vol, high div plus low correlation (latter only for Select Diversification) but additional thematic overlays," says Andreetto. "Background for the ESG/Low Carbon is client demand, as they wanted indices which follow the ESG and Low Carbon trend but are optimal to be used as underlying for structured products and not only ETFs. In this case it would not only be the extension of the SDS range but also an extension of our **Low Carbon and ESG offering**."

The **Stoxx Europe Diversification Select 50 EUR** which makes part of the Stoxx Diversification Select indices appears as the sole underlying of three structured products sold in the first quarter of this year in Belgium by BNP Paribas Fortis and Crelan, according to SRP which also shows that the index provider's **iStoxx series** have been deployed in almost 250 products and had over US$1bn in assets linked to structured products as of January 2016.

Other Stoxx smart beta indices beyond the 'customised range' featured in structured products include the **Eurostoxx 50 Daily Risk Control**; the **Eurostoxx 50 Risk Control 10%**; the **Eurostoxx Low Risk Weighted 50**; the **Stoxx Europe Low Beta High Div 50**; the **Stoxx Europe Maximum Dividend 40**; the **Stoxx Europe Sharpe Ratio 50**; the **Stoxx Global Maximum Dividend 40**; the **Stoxx Global Select Dividend 100**; and the **Stoxx Global Select Dividend Risk Control 10%**.

According to Andreetto, institutional investors are driving some of the initial focus on these strategies which started as satellite positions in their portfolios and are now being used as core positions. "This trend is also being manifested in the retail market where new generations of investors (Millenials) are now demanding such strategies," says Andreetto. "Because of this demand and the solutions being developed, we believe this segment will be more than just a complement in investors' portfolios. In addition, institutional and retail investors are now demanding indices that have an ESG or low carbon tilted version of the benchmarks. ESG and Low Carbon are substituting core benchmarks as long as there is not a significant deviation of the performance."

This shift in product demand has enabled the index provider to showcase its capabilities and provide a low carbon version of the Eurostoxx 50 index or an ESG optimised version. "We have also launched a fixed income and multi-asset versions of our flagship index (Eurostoxx 50 Corporate Bond Index,

Eurostoxx 50 Multi-Asset Indices and Eurostoxx 50 Multi-Asset Momentum Risk Cap Indices)," says Andreetto. "This exemplifies how our architecture can be used to build up on existing indexes and create new ones. We have developed a technology that allows us to be market agnostic and add value not just by providing a high quality dataset but also by delivering a higher potential for upside and outperformance in a unique way.

"These developments also show that innovation is accelerating rapidly and those providers that can react to demand in a timely manner will be better positioned to capitalise on new opportunities," says Andreetto.

"Our SDS range has also been set up in a way that can be dynamically adjusted to capitalise on market conditions," he says. "This is to do with the way we have developed our framework ... we created a matrix with all the different variables of Black & Scholes (market level, interest rates, dividend, volatility...) and we can offer different solutions to meet different expectations) and the corresponding indexes that will filtering in according to the expectations which then are matched with the appropriate payoffs."

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