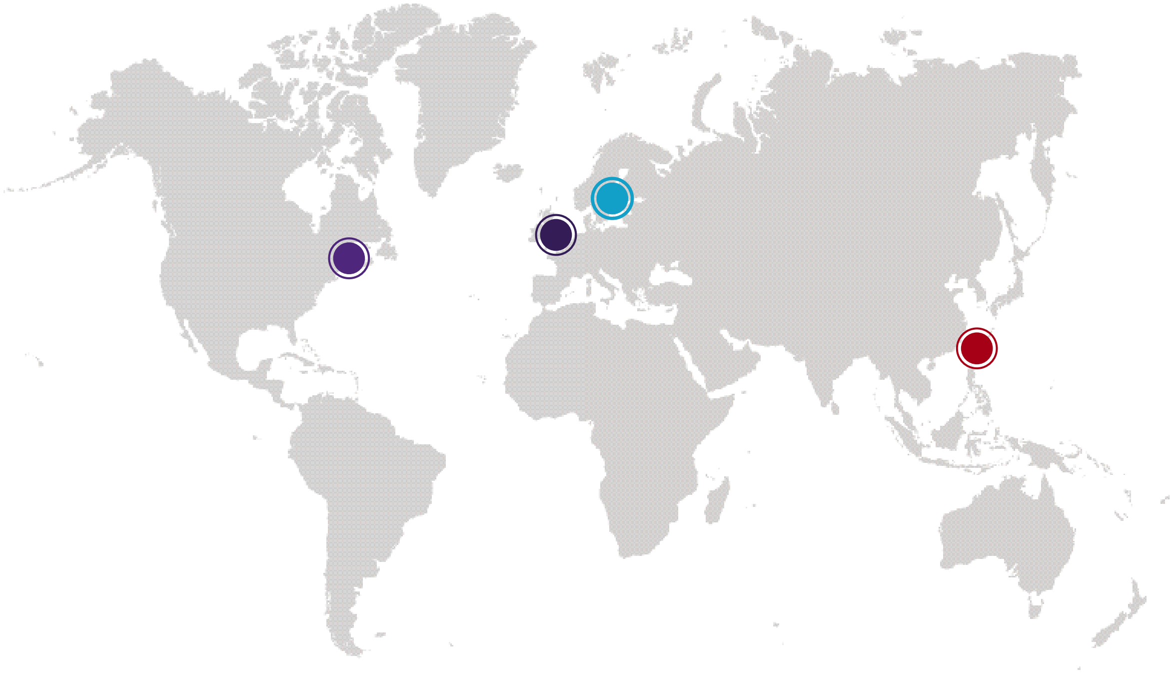
SRP Structured Retail Products
SPECIAL ISSUE

STOXX

Best Index Provider for
the Derivatives Industry 2016

SRP CONFERENCES



Asia-Pacific
Structured Products & Derivatives
Conference **Hong Kong | 19 September 2016**

Europe
Structured Products & Derivatives
Conference **London | February 2017** (Date to be confirmed)

Nordic
Structured Products & Derivatives
Conference **Stockholm | June 2017** (Date to be confirmed)

Americas
Structured Products & Derivatives
Conference **Boston | June 2017** (Date to be confirmed)

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STOXX strategy, activities and the market

(above)
Matteo Andreetto,
Head of Index Services
at Deutsche Börse Group
and CEO at STOXX

At the beginning of March 2016, Deutsche Börse Group changed the leadership structure of its market data unit, bundling it into: regulatory, data, index (STOXX and DAX) and infrastructure.

SRP talked to Matteo Andreetto, formerly global head of sales, STOXX and now head of index services at Deutsche Börse Group and chief executive officer of STOXX about the index provider's strategy and its plans for the issuers that use its benchmark and DAX Indices as underlyings for financial products.

"My role is to ensure that there is continuity in Deutsche Börse's index business," said Andreetto. "Our strategy remains focused on increasing STOXX's penetration in alternative markets, such as Asia-Pacific countries, which has resulted in the opening of offices in Sidney and Tokyo over the past year."

As a provider of underlyings for the structured products market, the challenge for STOXX is "always to continue innovating" in "a very competitive area for index providers".

One of the company's strengths is its relationship with the academic world, according to Andreetto. "We want to continue to develop that side of the business, to get the best ideas and academic research to create strong branded products," said Andreetto, adding that product innovation and leveraging STOXX's expertise in different areas such as smart-beta are core in his mandate.

From a structured products perspective, STOXX had a very successful 2015 in terms of new products and licensing, with over 550,000 structured products on the DAX and 85,000 structured products on STOXX Indices, according to Andreetto. "Last year, we were able to increase our market share as an underlying provider for structured products beyond our core markets in Europe on the back of an increased interest from investors in our indices," said Andreetto. "The demand for both our European and global underlyings come especially from US and Asian investors."

Issuance and demand in 2016 has been slightly weaker so far but “this is happening across the market”, according to Andreetto. However, despite the slowdown in licensing activities, the company has focused most of its activities this year around the development of its indices on three initiatives “to continue bringing innovation to the market”.

The STOXX Low Carbon Indices have a different approach and were developed in collaboration with specialist partners, such as the emission-related data providers CDP and South Pole Group. Reducing carbon emissions is a global objective, and market participants look for fully tailored solutions to decarbonise their portfolios to address long-term climate risks, while participating in the sustainable growth of a low-carbon economy, according to Andreetto. The STOXX Global Climate Change Leaders Index, for instance, tracks companies that are leaders in mitigating climate change and are publicly committed to reducing carbon emissions.

STOXX’s second initiative came to light in April 2016, with the launch of the EURO STOXX 50 Corporate Bond Index, a new benchmark aimed at capitalising on the increasing demand for alternatives in the fixed-income market. “This is a traditional benchmark for fixed-income investors comprising the components of the EURO STOXX 50, but in a different asset class,” said Andreetto. “Investors get exposure to the same companies they would get through the EURO STOXX 50 Index, but with a bigger universe and from a fixed-income approach, as they represent the corporate bonds and the subsidiaries of those companies.”

The index is “very well diversified” and also “a very strong partner” for the EURO STOXX 50 Index, according to Andreetto. “When we were developing this index, we found that there was negative correlation between the equity and the corporate bond version, and we decided to launch the EURO STOXX 50 Multi-Asset Indices, cross-asset versions, which are a combination of the two indices, but with different gradation, allowing investors to capture cross-asset exposure and the negative correlation between the two different asset classes,” said Andreetto. “That’s the kind of innovation we are bringing to the market.”

The index is “a good example” of how STOXX develops its products “with the end investor in mind”, as are the STOXX Select and STOXX Diversification Select index families “which have been developed for structured products and ETF investors”, according to Andreetto.

Product Issuance

2015		2016	
DAX	528,418	DAX	160,541
EURO STOXX 50	82,784	EURO STOXX 50	31,526
Cac 40	39,343	Deutsche Bank	12,162
Volkswagen	36,084	BMW	9,029
EUR / USD	34,558	Daimler	8,881
Daimler	30,034	Bayer	8,544
BMW	27,733	BASF	8,440
Bayer	25,304	Thyssen Krupp	8,386
E.ON	24,648	Commerzbank	8,172
BASF	24,399	DJ Industrial Average Index	7,918
Others	1,066,373	Others	319,570
Total	**1,919,678**	**Total**	**583,169**

The Select and Diversification Select index families were introduced last October and extended in May 2016 with the creation of “baskets or underlyings that can target dividends and lower volatility, and deliver lower correlation as well,” said Andreetto. “This enables us to create what we call super-optionality, which is a very important aspect for increasing participation in the performance of the underlying indices for end investors, and to deploy different payoff profiles.”

Further innovation has come from adding economic exposure filters to indices, enabling investors to sharpen portfolio exposure to selected regions and improve asset allocation to de-risk portfolios.

The indices allow investments in predefined countries or regions by selecting companies that have a dominant economic exposure to the targeted area. “The STOXX True Exposure Indices have been well-received in the ETF space, and have also aroused interest from the structured products market, as they provide an alternative exposure to companies by measuring the way they derive their revenue and income,” said Andreetto.

This is part of a shift in the market, away from traditional benchmarks and towards different ways of measuring the companies and their activities, according to Andreetto.

REGIONAL EXPANSION

Like its competitors, STOXX has been busy responding to demand for customised quantitative investment strategies from providers of structured products and other index-linked instruments in Asia-Pacific, according to Andreetto. "In Japan, for instance, demand is more mixed and comes from structured products providers seeking to offer exposure to alternative weighting schemes and European underlyings," said Andreetto. "Japanese retail investors are quite sophisticated and want to get exposure to European assets through smart beta underlyings. We have signed a MOU with Mitsubishi UFJ Trust and Banking (MUTB) last year to create and market new smart-beta indices in Japan."

The US market has also been a focus for STOXX over the last year, and represents "a very promising opportunity" as suggested by the usage of the EURO STOXX 50 Index in the US retail structured notes market, according to Andreetto.

During the first half of 2015, the European benchmark was the most used underlying in the European structured products market as a result of continuing uncertainty about the economy of Greece and its exclusion of the euro (Grexit) as well as speculation about when the US Federal Reserve will increase interest rates. And, for the first time, the index was also the leading underlying with the highest sales volume in the US, while, in Canada, it regained traction, sitting securely in third place by measure of both volume ($434m) and issuance (50 products), as of the end of the third quarter of 2015, according to SRP data.

"[Demand] was driven by asset allocation needs from US investors in structured products seeking exposure to European equities, which has somehow slowed down this year because of the uncertainty around geopolitical issues," said Andreetto. "[In the US], at a product level, our focus has been leveraging our capabilities and experience in the structured products market in Europe to develop underlyings that suit the needs of investors in this market."

The UK exit from the European Union and the uncertainty around the future movement of interest rates in the US remain a concern in financial markets and that has had an impact on investors' appetite around certain structures and payoffs, resulting in a shift to asset allocation strategies.

Once these uncertainties are resolved, it will be easier to work out investor appetite, according to Andreetto. However, STOXX Indices seem to be well established in the US market. Year to date, over 280 products linked solely to the EURO STOXX 50 Index have been marketed in the US, with a sales volume of US$1.4bn; while another 274 products featured the European benchmark alongside other indices, representing $1.1bn in sales.

"As an index provider, however, our role is not to predict or have a view on how the market is going to behave, but to provide investors with the best investment tools to capitalise on their views and meet their investment needs," said Andreetto. "That is why one of our main activities has been around the development of new underlyings that can extract value from themes and trends."

From a regulatory standpoint, the new index regulation approved in May by the European Council, and which applies to all providers of benchmarks located within the European Union, but also third country benchmark providers, will improve the index market and provide a standard set of rules for all participants, according to Andreetto.

Under the new rules, all index providers offering benchmarks within the EU will have to meet certain provisions around transparency and methodology already proposed in 2014 by the International Organisation of Securities Commissions' (IOSCO) principles, while some issues around credit indices have been addressed and clarified, according to Andreetto. The European Securities and Markets Authority (ESMA) launched a consultation at the end of May, seeking: responses about the definition of benchmarks; the measurement of the use of critical and

> ***"We have invested significant resources to serve this market and we have a team of product developers dedicated to structured products . . . This has allowed us to consistently deliver innovation in this market. We have launched many indices specifically optimised to be used in structured products and develop derivative instruments."***

Global Sales Volumes (US$m) - Underlyings			
2015		**2016**	
FX Rate (Unspecified)	153,701	FX Rate (Unspecified)	32,730
CNY/USD	31,289	EURO STOXX 50	11,490
EURO STOXX 50	28,793	CSI 300 Index	10,560
Single Share (Unspecified)	19,328	Gold	9,397
EURO STOXX 50, HSCE Index, S&P 500	16,024	S&P 500	7,074
EURO STOXX 50, HSCE Index	14,683	Libor	5,250
Share Basket (Unspecified)	14,305	CNY/USD	5,200
Gold	13,936	Single Share (Unspecified)	4,071
S&P 500	13,019	Share Basket (Unspecified)	4,058
CSI 300 Index	12,055	Kospi 200	3,690
Others	271,389	Others	93,727
Total	**588,522**	**Total**	**187,248**

significant benchmarks; the criteria for the identification of critical benchmarks; the endorsement of a benchmark / family of benchmarks provided in a third countries; and transitional provisions. However, most of the provisions of the new rules do not apply to independent index providers, such as STOXX, as their indices are not exposed to any conflict of interest; they put significant effort in the robust calculation and maintenance of the indices; and have been providing reliable market information for decades. The indices of the STOXX index family are transparent, rules-based and based on transaction data of regulated markets.

"All major index providers have adopted the IOSCO principles and, as STOXX, we are fully compliant and independently audited," said Andreetto. "Regulation can be seen as an additional burden, but we generally support the spirit of regulation and believe that a good basis has already been created at STOXX to efficiently implement the EU regulation when it applies."

STRUCTURED PRODUCTS

Structured products and derivatives in general continue to be a very important market for STOXX, as shown by the amount of assets under management linked to its indices in Europe, where it has a leading market share, but also globally.

"We have invested significant resources to serve this market and we have a team of product developers dedicated to structured products," said Andreetto. "This has allowed us to consistently deliver innovation in this market. We have launched many indices specifically

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optimised to be used in structured products and to develop derivative instruments."

Deutsche Börse Group activities have been focused on the derivatisation of investment strategies, with the German group taking a leading role in the design and development of quantitative investment strategies within an open architecture framework, according to Andreetto. "This allows us to create instruments in the form of delta one products that can be used as an underlying for index-linked products and optimised in different forms as underlyings for structured products," said Andreetto. "Our work in the structured products market has given us the opportunity to interact with this segment of the market and understand that we can provide multi-optionality in a very efficient way. That's something that enables investors to get more participation in the potential upside of the strategy, while providers can also deploy different levels of protection, and payoff structures."

STOXX's indices "are designed for multiple usage" and there are multiple inputs in the STOXX factory, which has resulted in the creation of delta one instruments that go back into the structured products factory, according to Andreetto.

STOXX: Facts and figures

ORGANISATION

STOXX is part of Deutsche Börse Group

Deutsche Börse Group covers the entire trading value chain and has a wide spectrum of services

STOXX runs a leading global index offering – differentiating by innovation, quality and liquidity

Headquartered in Zurich, with offices in Frankfurt, London, New York, Sydney and Tokyo

All STOXX and DAX indices are fully rules-based, with rules disclosed in methodology guides

STOXX has been at the forefront of innovation since creating the market's first Eurozone blue-chip index in 1998 and has won many innovation awards

Major divisions: product development, index operations, market development, research and sales

STOXX calculates a comprehensive index family across the world of over 7,500 indices. Best known for the leading European equity indices the EURO STOXX 50, STOXX Europe 50 and STOXX Europe 600, the index provider and specialist maintains and calculates its global index family, which consists of total market, broad and blue-chip indices for the Americas, Europe and Asia / Pacific regions and Latin America and BRIC (Brazil, Russia, India and China) sub-regions, as well as global markets. STOXX indices are licensed to more than 500 companies globally, a list that includes the largest financial products issuers, capital owners and asset managers. The indices are used as underlyings for financial products, such as ETFs, futures and options and structured products, and also for risk and performance measurement.

MAIN AREAS OF GROWTH AND DEVELOPMENT

- Since the global expansion which started in 2010, STOXX is globally well positioned and has a very strong position in Europe.
- Additionally great successes in Asia and US with the launch of innovative products and flagships.
- STOXX will continue to expand their strong position in Europe but also globally.
- Further development of the STOXX index family, regional but also thematic (such as smart beta).
- STOXX's smart beta indices are based on alternative weighting rather than free float market capitalisation and cover different strategies, and are available for different regions and countries.
- Introduced the STOXX GC Pooling index family in 2013 as the need for an independent benchmark based on secured transactions grew in the wake of the Libor scandal.
- The focus is clearly on innovation, which has been shown with the most recent product launches.
- Developed the STOXX True Exposure index family in June 2015, the first global offering that allows investors to gain exposure to a pre-defined country or region that limits their exposure to foreign currency and market risks.
- Launch of the STOXX Low Carbon indices, among them the STOXX Global Climate Change Leaders in February 2016.
- STOXX entered the multi-asset in April 2016 with the introduction of the EURO STOXX 50 Corporate Bond Index, followed by the launch of the EURO STOXX 50 Multi-Asset Indices in May 2016.
- STOXX announced, at the end of May 2016, an extension of the STOXX Select and STOXX Diversification Select index families that were introduced in October 2015. The newly launched indices combine investment themes, such as Low Carbon and ESG, with low volatility, high dividend and low correlation screens, creating hybrid index concepts.

More info

www.stoxx.com/company-profile

MAJOR BENCHMARK INDICES

- EURO STOXX 50
- STOXX Europe 50
- STOXX Europe 600
- STOXX Global 1800
- STOXX Global 3000
- STOXX USA 900
- STOXX USA 50
- STOXX Asia / Pacific 600
- STOXX Japan 600
- STOXX China A 50
- STOXX Emerging Markets 50

MAJOR NEW INDICES

- STOXX Low Carbon Index Family
- STOXX True Exposure Index Family
- STOXX Select and Diversification Select Index Family
- EURO STOXX 50 Corporate Bond Index
- EURO STOXX 50 Multi-Asset Index

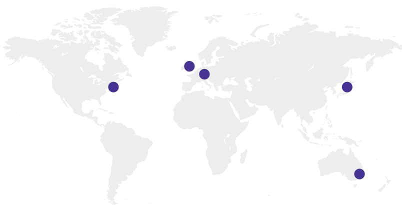
VOLUME OF ASSETS UNDER MANAGEMENT INVESTED AGAINST STOXX INDICES

- ETFs: 268 products listed globally with AUM of US$110bn (as at April 2016)
- Structured products (as at April 2016):
    - > Issued products on the DAX: 155,643
    - > Issued products on the STOXX: 35,710
- Derivatives (as at April 2016): $306.72m traded contracts

Top three business types using STOXX indices:

- ETF providers
- Structured products desks
- Asset managers

KEY PERSONNEL



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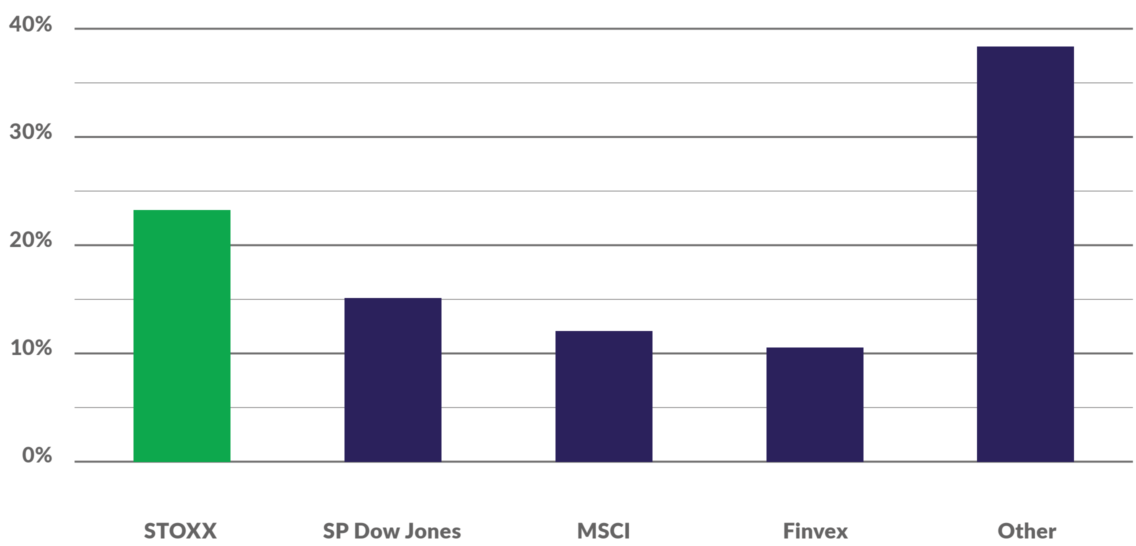
Best Index Provider for the Derivatives Industry

Responsiveness, market insight and commitment to innovation has propelled STOXX to the top of the pecking order for banks, platforms, wealth managers and independent financial advisers seeking to develop index-linked products across all markets. According to the latest SRP Awards surveys, which polled Europe, Middle East & Africa (Emea), Asia-Pacific (Apac) and the Americas, STOXX took nearly a quarter of all votes, and 50% more than the next competitor. The findings of the SRP poll suggest that STOXX is the first choice for structured products issuers for its responsiveness to client's needs and demands, its commitment to establish long-lasting relationships and its approach to innovation and providing answers to investors' needs.

Despite having the European market as its natural domain, STOXX has expanded its activities to other jurisdictions and has become the preferred provider beyond the Emea region, establishing itself as the first European index provider in Apac and the Americas. In North America, STOXX has become, in recent years, the second most popular underlying as suggested by sales of structured products featuring the EURO STOXX 50, overtaking other domestic indices, such as the Russell 2000 and Canada's S&P / TSX 60 Index.

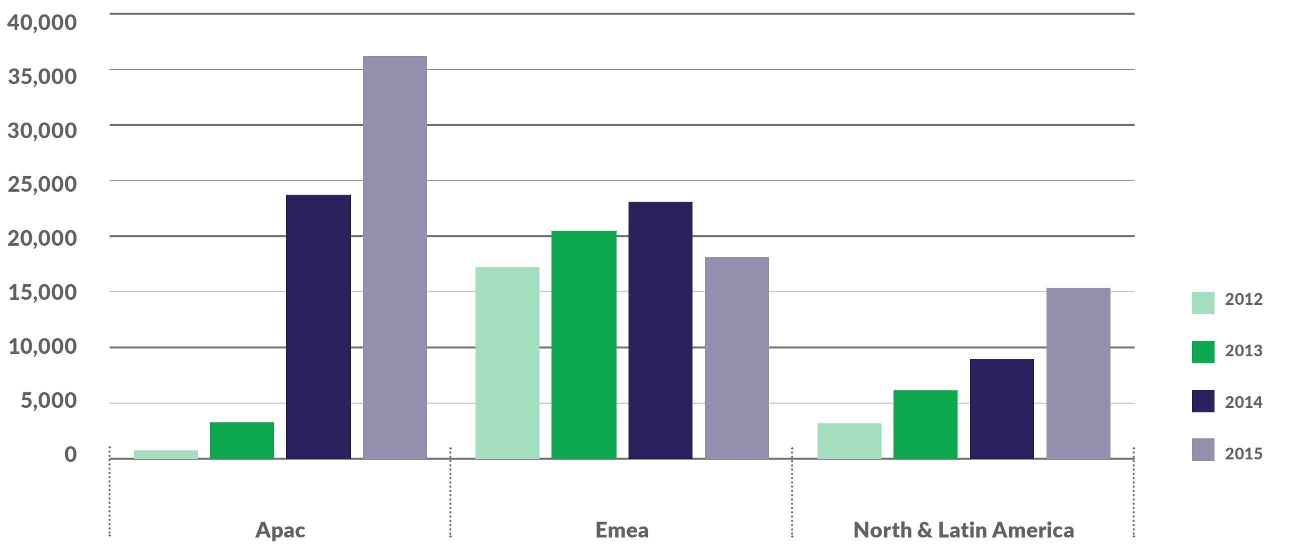
Number of votes (Emea, Americas and Apac)



Source: StructuredRetailProducts.com

With a 371% increase between 2012 and 2015, the EURO STOXX 50 became the leading underlying in the US in the second quarter of 2015, taking the highest sales volume for the first time in the US market. Sales of products linked to the European benchmark index in 2015 saw a 53% rise on the year. In Canada, the European index also regained popularity, sitting in third place by volume ($434m) and issuance (50 products).

EURO STOXX 50 Index - Sales (US$m) 2012-2015

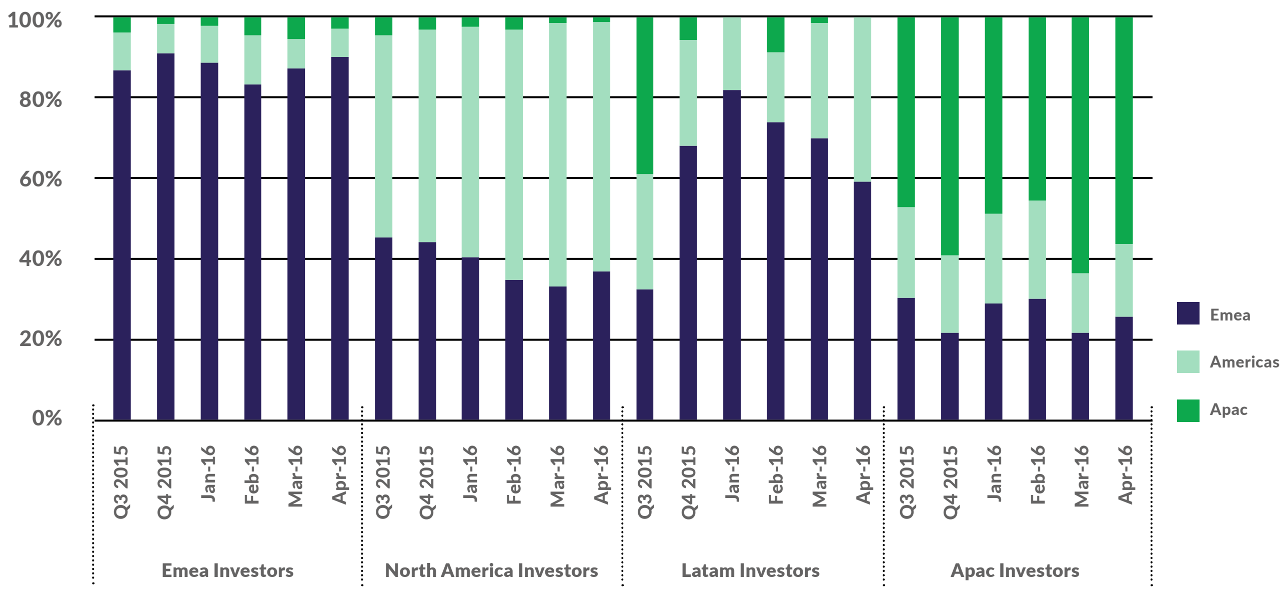


Source: StructuredRetailProducts.com

The spike in the implied volatility of the EURO STOXX 50 in the first half of 2015 resulted in attractive pricing and the ability to provide cheaper options to structure more attractive products, largely featuring an enhanced upside with a cap. In addition, the EURO STOXX 50 also offered exposure to the Eurozone economy and the possibility of hedging out foreign exchange risk, two features that proved attractive to investors in the US.

Last year, STOXX's market share was further boosted by the expansion of EURO STOXX 50 in Apac. Used mostly as a component of baskets and for diversification purposes, the index became increasingly popular with issuers in South Korea, which, on its own, represented 90% of the whole STOXX-linked issuance in the region over the last 12 months. At the same time, sales of products linked solely to the EURO STOXX 50 in Apac amounted to US$2.1bn.

Index Provider by Region



Source: StructuredRetailProducts.com

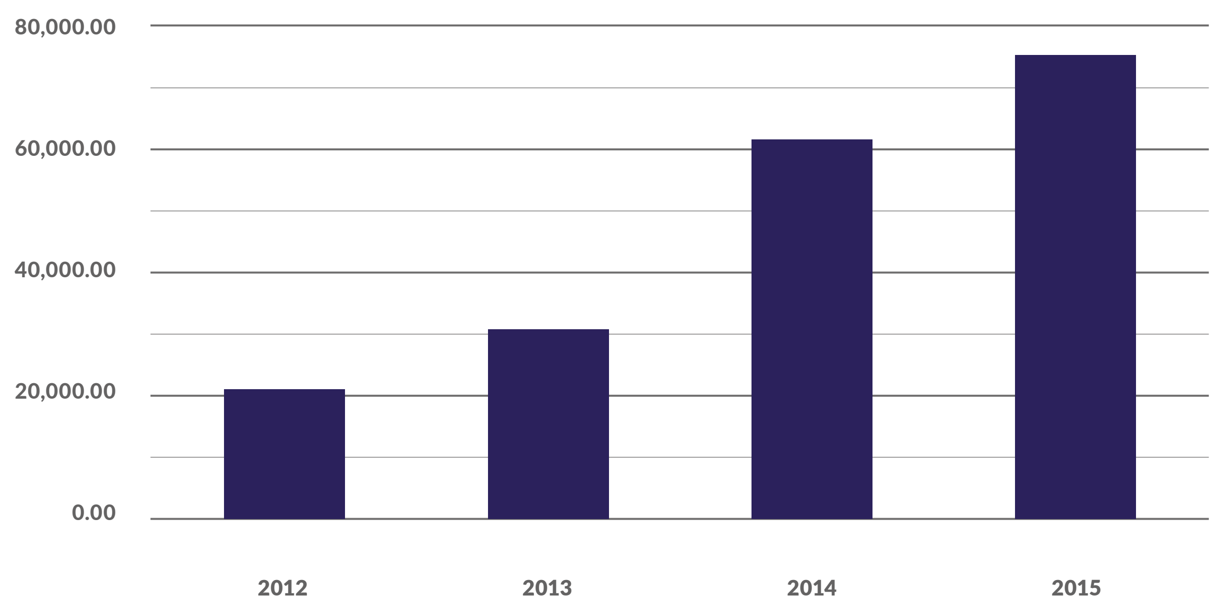
In Japan, products linked to the index also gained increasing traction in the second quarter of 2015, as investors sought to capitalise on the relatively low entry level and bullish outlook following the launch of a quantitative easing programme by the European Central Bank (ECB). With a 37% year-on-year increase, the Japanese market was the second driver of STOXX's expansion in the region, with the index provider also partnering with local providers, such as the Mitsubishi UFJ Trust and Banking Corp (MUTB), to launch the iSTOXX MUTB Japan Quality 150 Index in August 2015.

10 TIMES THE OVERALL MARKET GROWTH

Between 2012 and 2015, the popularity of STOXX's underlyings has been steadily increasing, marking a 257% increase across all regions against 27% global market growth for the same period, according to SRP data.

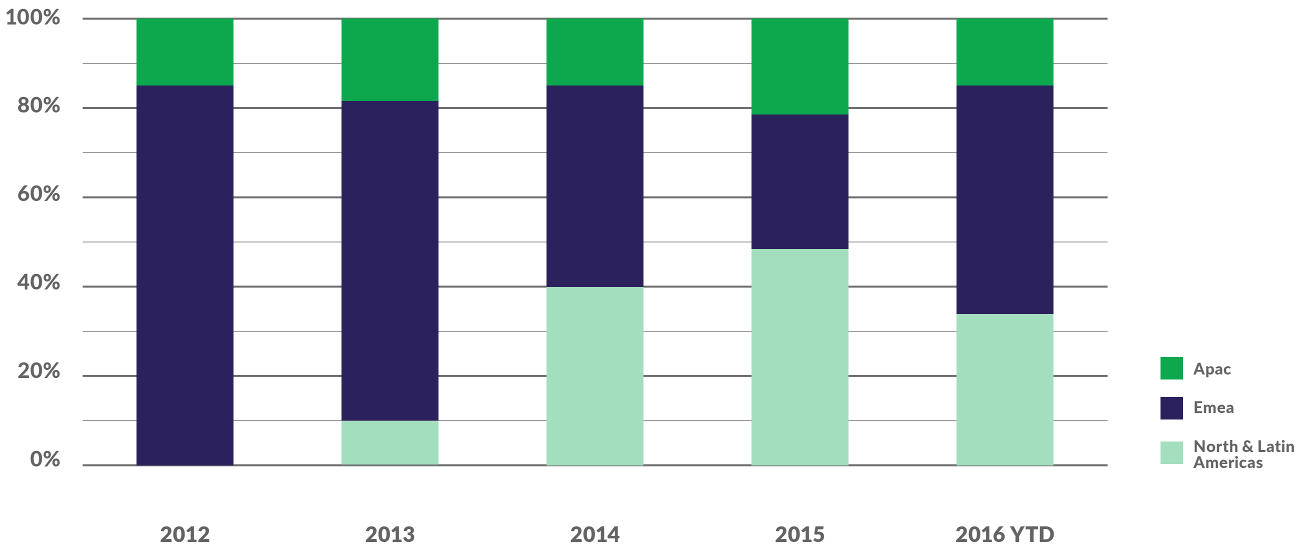
SRP data reveals that the EURO STOXX 50 Index was the most popular sole underlying for structured products globally between April 2015 and April 2016, with nearly 3,000 products featuring the European equity index, and was used in combination with other indices in thousands of products across markets. As a standalone asset, the EURO STOXX 50 accounted for 89% of all sales of structured products linked to STOXX underlyings for the same period. Other STOXX indices, such as the EURO STOXX Select Dividend 30, Euro iSTOXX Equal Weight Constant 50, STOXX Global Select Dividend 100 and EURO STOXX Banks completed STOXX's list of bestselling underlyings for 2015, with a combined 7.6% of sales.

Sales of STOXX Underlyings 2012 - 2015 (USDm)



Source: StructuredRetailProducts.com

Sales of STOXX Underlyings 2012 - 2016

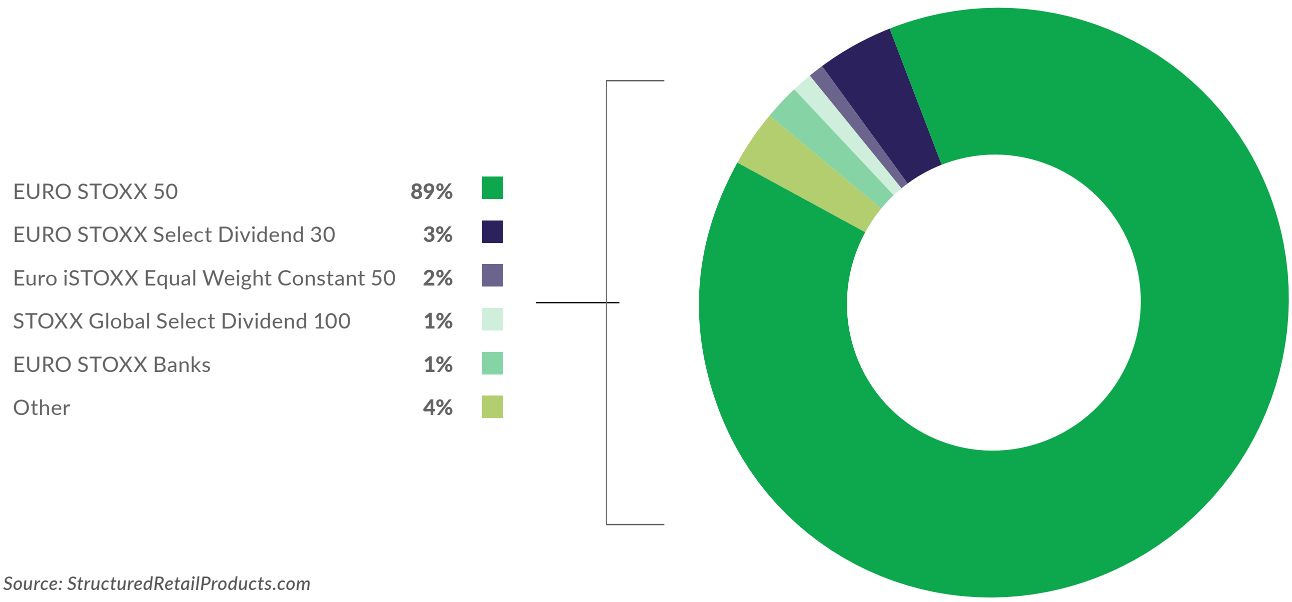


Source: StructuredRetailProducts.com

FROM SIMPLICITY TO SMART INVESTMENT STRATEGIES

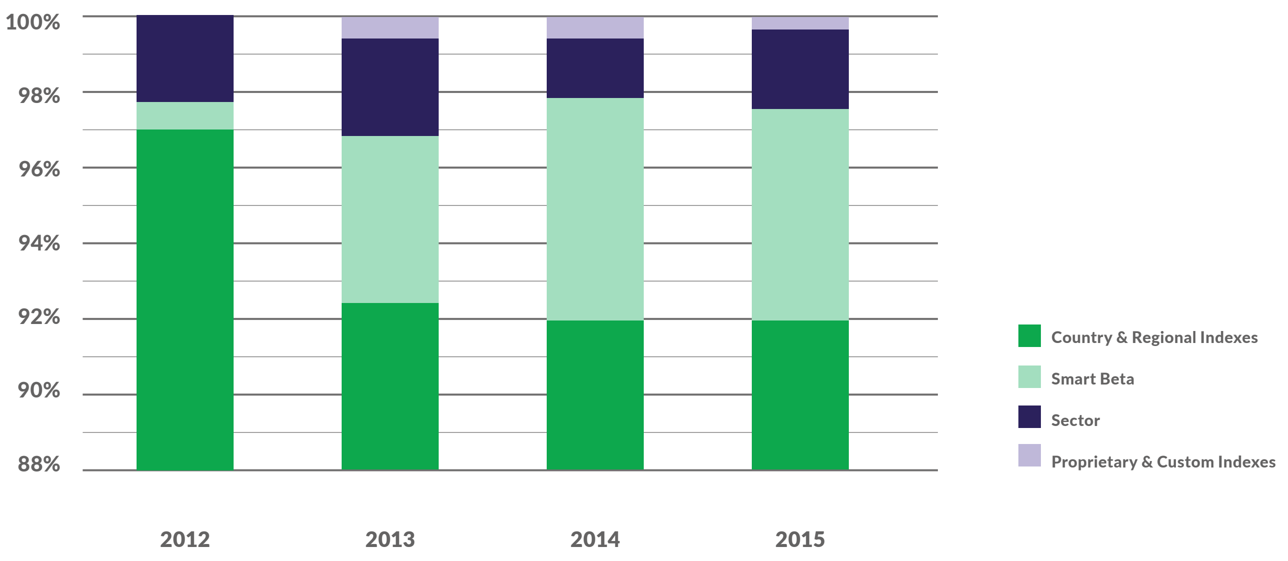
Despite the dominance of STOXX's standard Country & Regional indices, which survey respondents praised for their strict rules-based methodology, the period after 2012 saw an increase in demand for the index provider's range of smart beta indices, marketed under the iSTOXX sub-brand. STOXX identified the market need for strategy investment underlyings after market volatility exposed the limitations of traditional market cap-weighted indices to deliver consistent returns, and responded by developing new indices based on non-market cap–weighted concepts such as factor investing and apply filters to its benchmarks (low volatility, high dividend yield, or low correlations). This move did not go unnoticed by the structured products market which saw the issuance of capital-protected retail structured notes and certificates linked to strategy indices doubling in 2014, on $1.5bn in sales.

STOXX top 5 selling indices April 2015 – April 2016



Source: StructuredRetailProducts.com

Sales of STOXX indices by category 2012 - 2015



Source: StructuredRetailProducts.com

Since then, STOXX has expanded its range of strategy indices, such as the STOXX Select and STOXX Diversification Select index families, which were introduced in October 2015 provide low volatility, high dividend and low correlation screens within an attractive pricing framework specifically designed as liquid underlyings for financial products, such as structured products and exchange traded-funds.

STOXX's portfolio of benchmarks is completed by indices specifically developed in partnership with and for clients, namely the 'STOXX Customized' range which never carries the STOXX brand in the index name. Examples of such indices include but are not limited to Index Euro Actions, GT 30 and ECO 10.

Index category	2012 USDm	2013 USDm	2014 USDm	2015 USDm	% Increase 2012-2015
Country & Regional Indices	20,688	30,312	56,634	70,753	242%
Smart Beta	227	1,567	3,422	3,838	1,589%
Sector	467	799	1,285	1,738	272%
Proprietary & Custom Indices		82	129	24	

Source: StructuredRetailProducts.com

Deutsche Börse's STOXX features in over 140,000 structured products that are still live globally. Germany (110,777) has the highest number of products featuring STOXX's underlyings, followed by Austria (76,988) and South Korea (15,420). The most active providers of products linked to STOXX's indices are Deutsche Bank (20,816), followed by Societe Generale (14,269) and BNP Paribas (13,646). The German group also manages the DAX indices, which underlie over 900 live products. The index provider's iSTOXX series has appeared in almost 250 products and is the underlying for over US$1bn in assets linked to structured products as of January 2016. Other STOXX smart beta indices featured in structured products include:

- EURO STOXX 50 Risk Control
- EURO STOXX 50 Risk Control 10%
- EURO STOXX Low Risk Weighted 50
- STOXX Europe Low Beta High Div 50
- STOXX Europe Maximum Dividend 40
- STOXX Europe Sharpe Ratio 50
- STOXX Global Maximum Dividend 40
- STOXX Global Select Dividend 100

Q&A with

Jan-Carl Plagge

Jan-Carl Plagge is a director and head of applied research at STOXX, and responsible for the development of innovative index concepts across all asset classes. Prior to joining STOXX, Plagge was a product development manager at Deutsche Börse, where he was involved in the development of equity and strategy indices.

SRP spoke to Plagge about the most recent developments and innovations around STOXX's family of indices, and what strategies will be applied in the structured products market.

The equity market continues to be the main driver of activity in the index market. However, there has been a recent shift to the use of strategies to extract value from the equity market and an increasing emphasis on other asset classes, such as fixed income. What is STOXX offering in these two areas?

It is important to differentiate between asset classes and strategies. STOXX is one of the leading index providers globally, with a strong emphasis on equities. However, more recently, we have expanded our offering into fixed income and bonds with the recent launch of the EURO STOXX 50 Corporate Bond Index, which allows investors to take positions in the bonds of the 50 most well-known Eurozone blue chips. On top of that, we have also launched the EURO STOXX 50 Multi-Asset Indices, a series of cross-asset class benchmarks based on the EURO STOXX 50 and the EURO STOXX 50 Corporate Bond Indices which offers different allocations between bonds and equities, depending on the risk profile of investors.

When it comes to strategies, we have a very comprehensive range of indices, most of which are based on the STOXX Global Total Market Index, which spans the entire world of investable equities, covering around 95% of the investable free-float market capitalisation. We then slice and dice that underlying universe, which covers over 7,000 stocks from different regions and sectors to build country and sector indices, and regional benchmarks. Additionally, we have an extensive range of theme-based indices, such as our STOXX Global Broad Infrastructure Index, which we licensed to FlexShares in the US for an exchange-traded-fund (ETF) in 2014; and, in smart beta, we have also introduced new gauges, such as our minimum variance indices and our recently launched iSTOXX Europe Factor Indices.

Another area of focus for STOXX is ESG and low carbon. We introduced, in February 2016, the STOXX Low Carbon Index family, which offers varying degrees of carbon exposure through four sub-families to enable market participants to limit the exposure of their portfolios to carbon risk while participating in the low-carbon economic growth. This family was designed to act as an underlying for ETFs and other investable products, such as structured products and derivatives.

We have also combined our ESG and smart beta capabilities to develop indices, such as the iSTOXX Europe ESG Select 30 Index, which was licensed by JP Morgan for the launch of an index linked green bond in partnership with the World Bank. The iSTOXX Europe ESG Select 30 Index screens European companies from the STOXX Global ESG Leaders Index for those that pay high dividends and also have low volatility, resulting on a hybrid portfolio of ESG, high dividend and low volatility strategies.

Where is investors' appetite at the moment?

We see a huge trend around two topics. One is sustainable investment, which has resulted in an increased demand for our ESG and low carbon indices. The other is a big shift away from traditional market cap-weighted indices. These two relatively new trends are independent of individual countries, however, in ESG, we see slightly more interest from outside Europe, whereas, in smart beta and multi-sector, demand is evenly distributed across regions.

What do structured products desks want in the current environment? Is the pricing (low interest rates) influencing the requests you get from product providers? Can index providers build indices that address the need for capital protection and income?

The low interest rates environment has affected many investment products and structured products in particular because of capital protection. This is a concern, because it limits the ability to provide upside and capital protection. However, STOXX has been working to develop customised indices with a focus on low risk or minimum variance filters. Volatility influences the price of options on any given underlying. So, the higher the volatility, the more expensive the option and the less room to offer upside on the performance of the underlying. The rationale behind our low risk indices is to bring down the price of the option which, in turn enables investors to increase participation in the performance of the underlying index.

We have been doing this with our risk control indices. From an income perspective, we offer our STOXX Select Dividend and STOXX Maximum Dividend Indices, which are aimed at maximising the component's dividend yield with a clear focus on generating income. Our low volatility and minimum variance indices, on the other hand, are geared to reduce total risk in the form of standard deviation and also display a lower drawdown. This is not capital protection per se, but it is a way of reducing the risk and the fluctuation of the underlying. On the subject of capital protection, we can also combine plain vanilla equity indices with options. As part of our relationship with Deutsche Börse Group, we have developed a number of indices over the years, such as the DAXplus Protected Put Index, which is a benchmark that combines long investments in the DAX with a long investment in a put option based on the DAX. By combining these two elements, the investment is protected against downside risk, because, whenever then index falls below a certain point, the put option gains in value, compensating for the fall in the value of the index. These are elements, we, as an index provider, can deploy to customise our indices for particular products.

There is a lot of talk in the market about smart beta, with some claiming that this is just another marketing fad. What is your take on these strategies?

There has been a huge demand for smart beta indices over the last two years. Investors have become aware of certain deficiencies related to standard market indices and are increasingly seeking alternatives. The use of smart beta indices will increase. We follow a standard definition, which considers smart beta indices as strategies that attempt to gain systematic exposure to well-known factors, such as value and growth, with the aim of gaining compensation or premia for the exposure to those sources of risk.

In that context, we have developed a series of single-factor indices, such as our STOXX Minimum Variance Indices, and they are aimed at minimising the overall volatility or standard deviation of our indices. To name another example, the iSTOXX Europe Multi-Factor Indices aim at capturing risk premia, not only from one source of risk, but from a broader range of risk factors.

Is this trend here to stay or could we be talking about a new trend after the next market correction? Are there any pitfalls around investing in smart beta?

> ***"We see a huge trend around … sustainable investment… and a big shift away from traditional market cap-weighted indices."***
>
> Jan-Carl Plagge, Director and Head of Applied Research at STOXX

Smart beta is here to stay despite the feeling this may be a short term trend. Research around factor investing shows that there are systematic effects of risk factors on asset prices. Thus, it's not marketing noise, i.e. random fluctuation. However, it is important to mention that the use of smart beta indices is no guarantee for outperformance relative to a traditional market-cap weighted index or relative to a broader market exposure. Some smart beta indices may lag behind cap-weighted indices in certain market environment. Investors need to understand that risk premia also fluctuates over time. This has resulted in the development of multi-factor indices aimed at diversifying the exposure of the index to more than one source of risk.

What other area do you see getting traction in the short term?

We think ESG will continue to drive a lot of activity in the short term and especially the long term. In addition, we have been working on some strategies, such as the STOXX True Exposure Indices, which are a more efficient way to construct regional indices that enable investors to capitalise on short-term trends.

In the selection process for those indices, we apply different filters with a focus not only on a company's country of incorporation, but also on its regional sources of revenue generation.

In this context, last year we launched our EURO STOXX International Exposure Index, which tracks companies domiciled in the Eurozone that generate a large proportion of their revenues outside the Eurozone. The index has been licensed to Source as the underlying for an ETF in May 2015. Our research shows that these companies tend to outperform the benchmark, ie. the EURO STOXX, when the euro depreciates, and vice versa. As those companies generate the majority of their income outside the euro region and in other currencies, such as the US dollar, they provide good potential for diversification and an implied currency hedge.

Before the crisis, the structured products market saw an increasing number of theme-based indices, but that changed after the crisis. Is this kind of indices coming back or will they remain a marginal way of diversifying investment portfolios?

Themes remain very important for investment products, especially structured products. At the moment, a lot of the activity and sales are driven by ESG and low carbon strategies. When it comes to assessing whether such strategies can be applied for diversification purposes, these ones are analysed much more closely. Investors want to understand what the underlying drivers of risk and return are, in order to establish if a certain theme would fit with their investment goals.

Another topic of interest is strategies that aim at exploiting the benefits that may arise from demographic change. We have received requests from structured products providers for demography-based indices, and we launched the iSTOXX Europe Demography 50 Index to respond to that demand. The index was licensed to Credit Suisse and was used in a number of structures. This index offers exposure to the demographics of developed markets with populations that are expected to become older on average. The index overweights those industries that are expected to profit from that demographic trend, such as the healthcare sector, infrastructure sector and so on.

Proprietary indices developed and designed by investment banks continue to be used as an alternative to offer greater yields and avoid the payment of licensing fees. However, because of conflicts of interest, some investment banks are offloading parts or their whole indexing capabilities. Can index providers capitalise on this?

Investment banks outsourcing their index units is something we have seen for a while now. This may not only be initiated by the benchmark regulation, but also due to banks' own far-ranging review of businesses exposed to regulatory pressures in general. Given our capacities as an independent index provider, we are a neutral partner when it comes to developing investment products and we are an obvious partner to then take on these units, with no conflict of interests. ■

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