

The EDHEC European ETF and Smart Beta Survey

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Introduction

- ETF industry has undergone rapid growth since the first European ETF was traded in 2000.
- Assets under management of the 1,560 ETFs amounted to \$552 billion at the end of December 2016 (ETFGI, 2016).
- Nowadays, growing demand for indices as investment vehicles has led to innovations including new weighting schemes and alternative definitions of sub-segments.
- European smart beta ETFs AUM reach €27.4 bn at the end of 2016 and accounted for 12% of the total assets (Lyxor, 2017).
- The aim of the survey is to analyse investor motivations for investing in those products and the issues investors are facing.



Outline

- The Survey: A Unique Source of Insights
- How do investors select and use ETFs?
- What are the key objectives driving smart beta strategies?
- Future developments



- **The Survey: A Unique Source of Insights**
- How do investors select and use ETFs?
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Potential for Unique Insights (I)

- Access to **differentiated** information from investors:
 - The dominant purposes of ETF usage
 - How do investors select ETFs
 - What are the motivations for investing in smart beta strategies
 - How do investors implement smart beta strategies (replication vs discretionary)
 - Do investors have the necessary information to implement smart beta strategies
 - What requirements have investors for selecting factors in factor-based strategies?



Potential for Unique Insights (II)

- The survey allows obtaining **forward-looking** information:
 - ETF future growth drivers
 - Growth prospects for smart beta
 - What are investors expectations for further developments for ETF products
 - Expectations on future developments for smart beta products



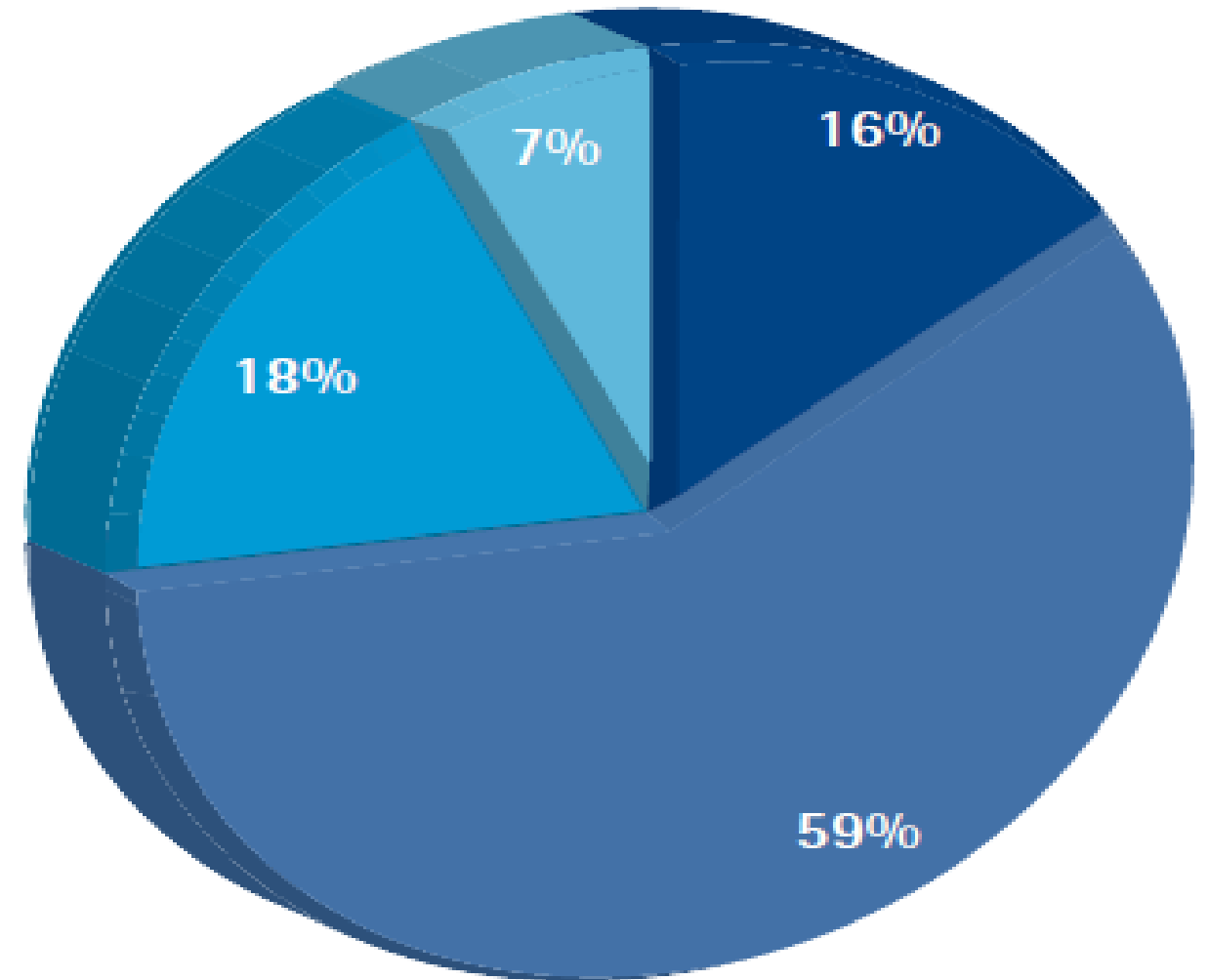
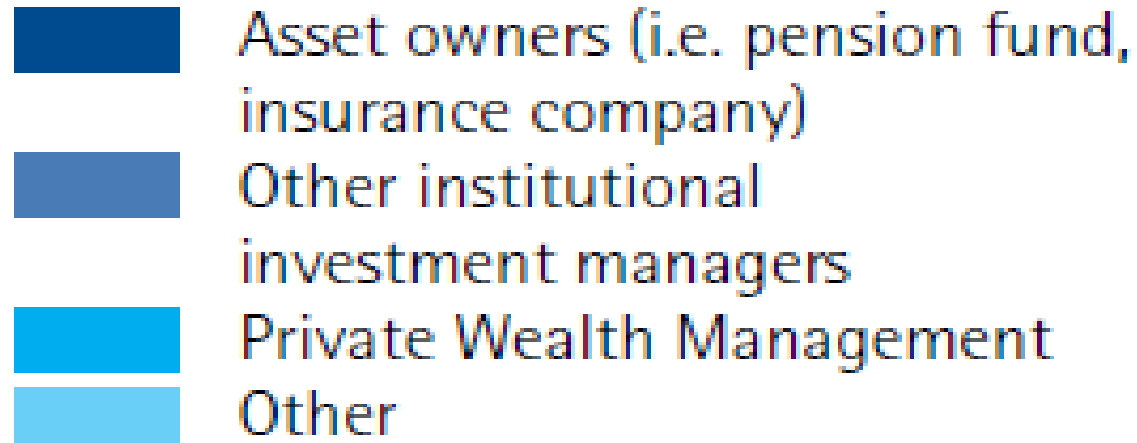
Scope of the Survey

- Conducted among investment professionals
 - from December 2016 to February 2017
 - by online questionnaire
- The 211 respondents together have at least €3.7 trillions of AUM¹.
 - 61% of respondents have AUM > €1bn
 - 39% of respondents have AUM > €10bn
- Respondents span 27 European countries
 - 19% are from the UK, 16% from Switzerland, 60% from European Union members and 5% from other countries outside EU.

1. To be compared with a total AUM of €22.8 trillions in Europe at the end of December 2016 (EFAMA , 2017).



Main Activity of Respondents' Institution

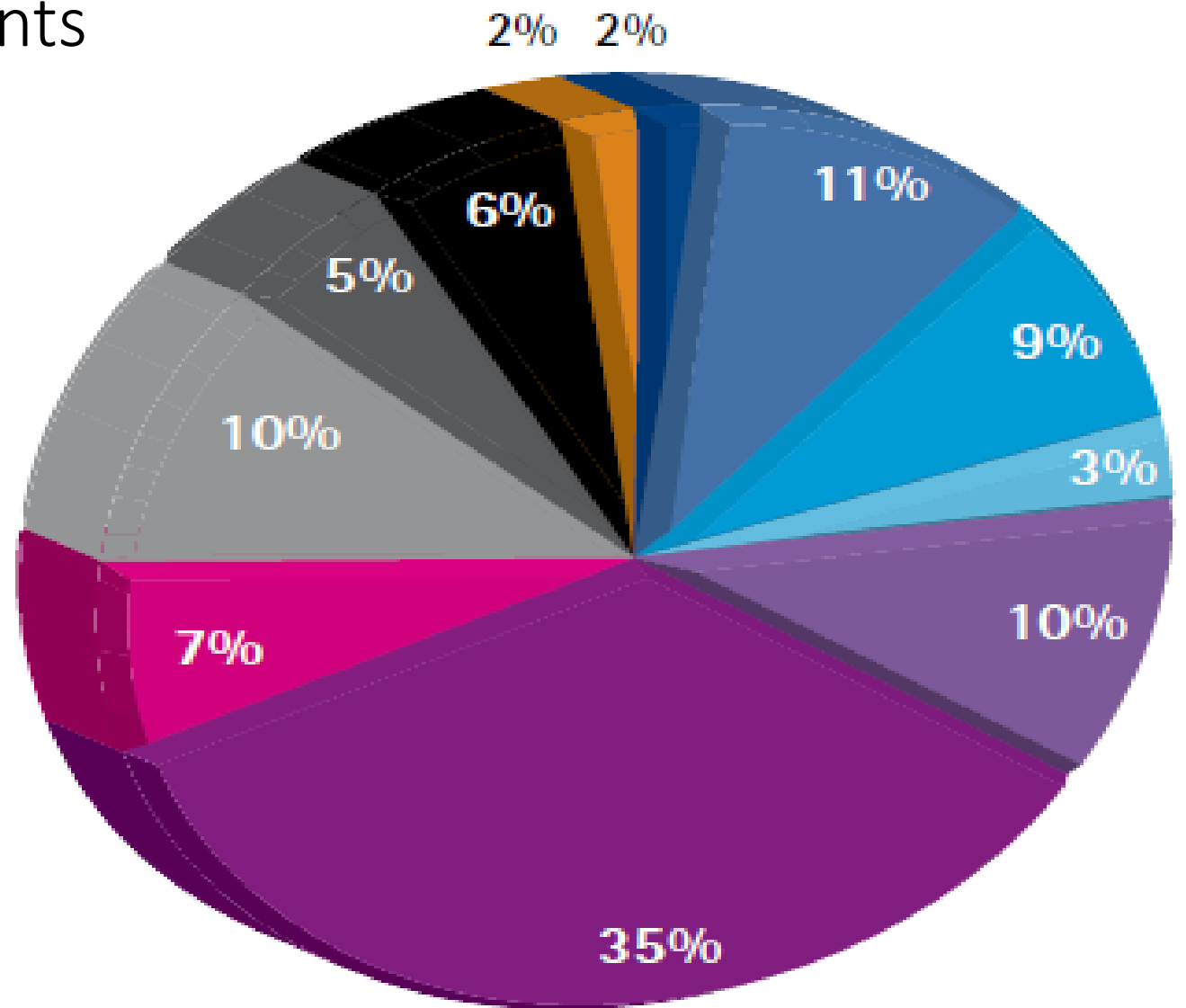


- Main focus on institutional investment management

Function of Survey Respondents

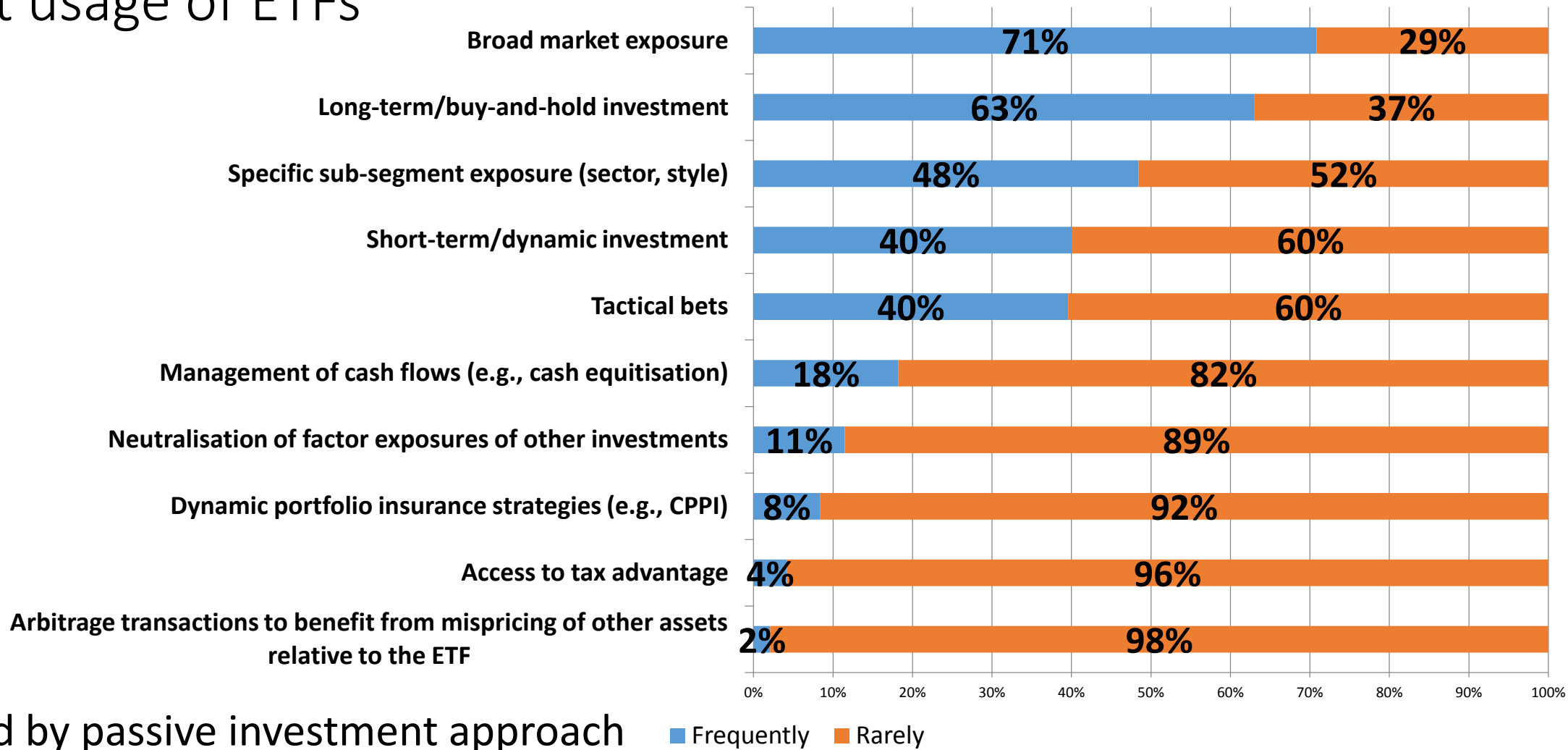


- Main focus on investment decision makers



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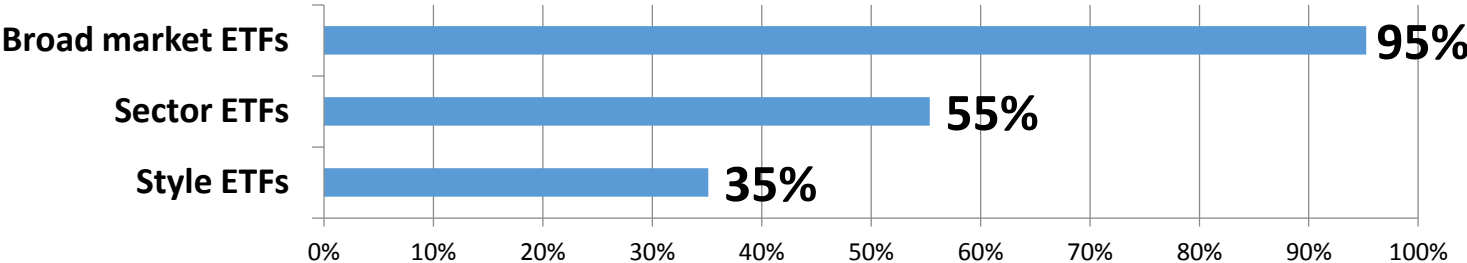
Current usage of ETFs



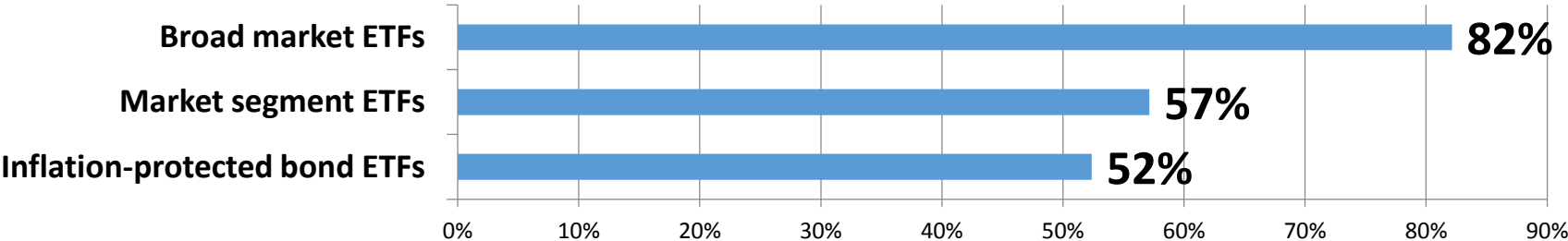
- Dominated by passive investment approach
- Broad market exposure is the main focus

Preference for broad market exposure

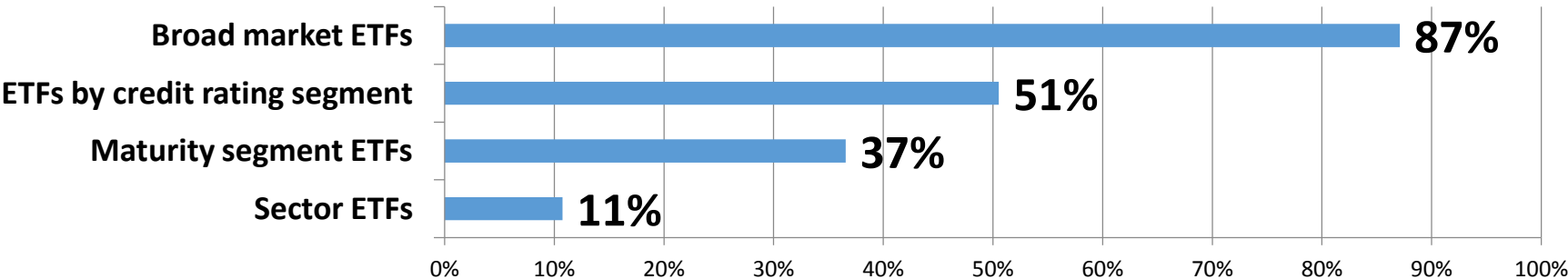
Equity Investments



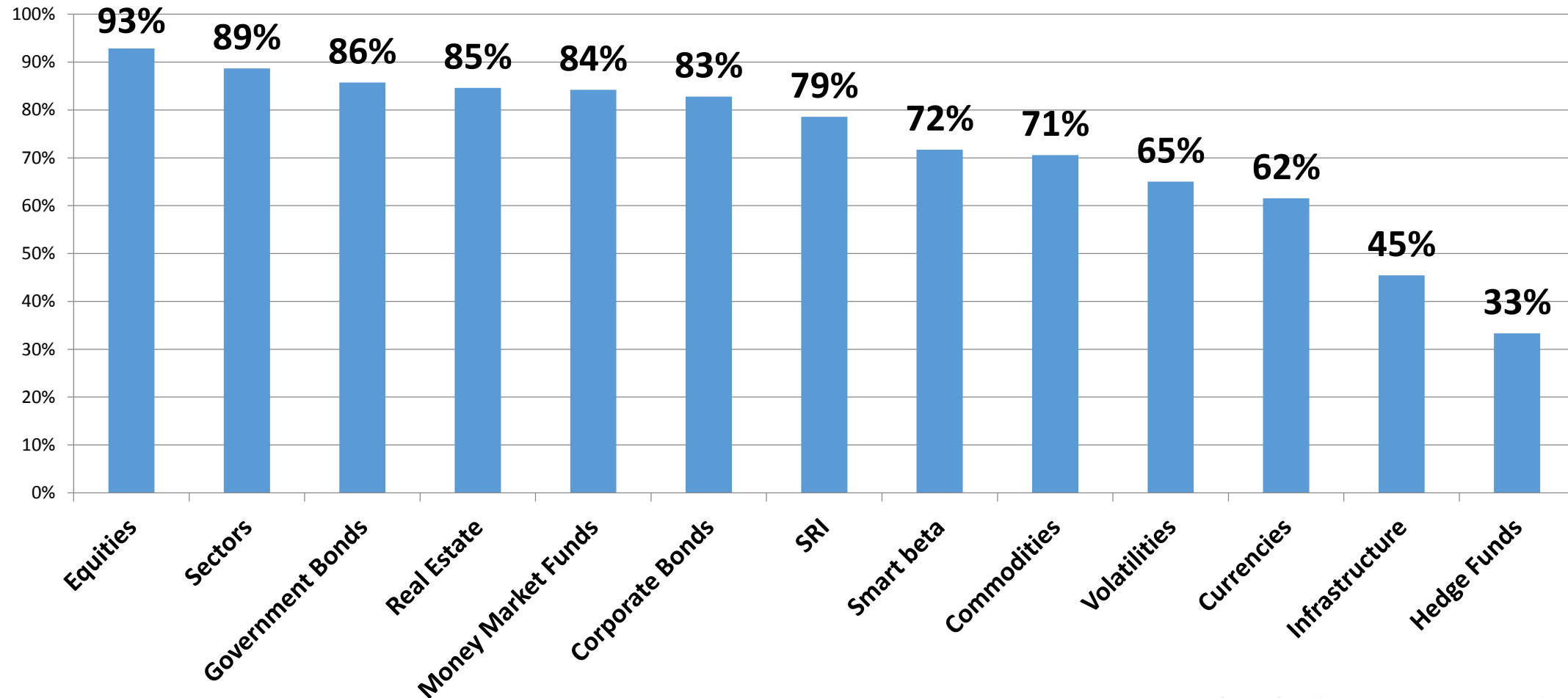
Government Bond Investments



Corporate Bond Investments



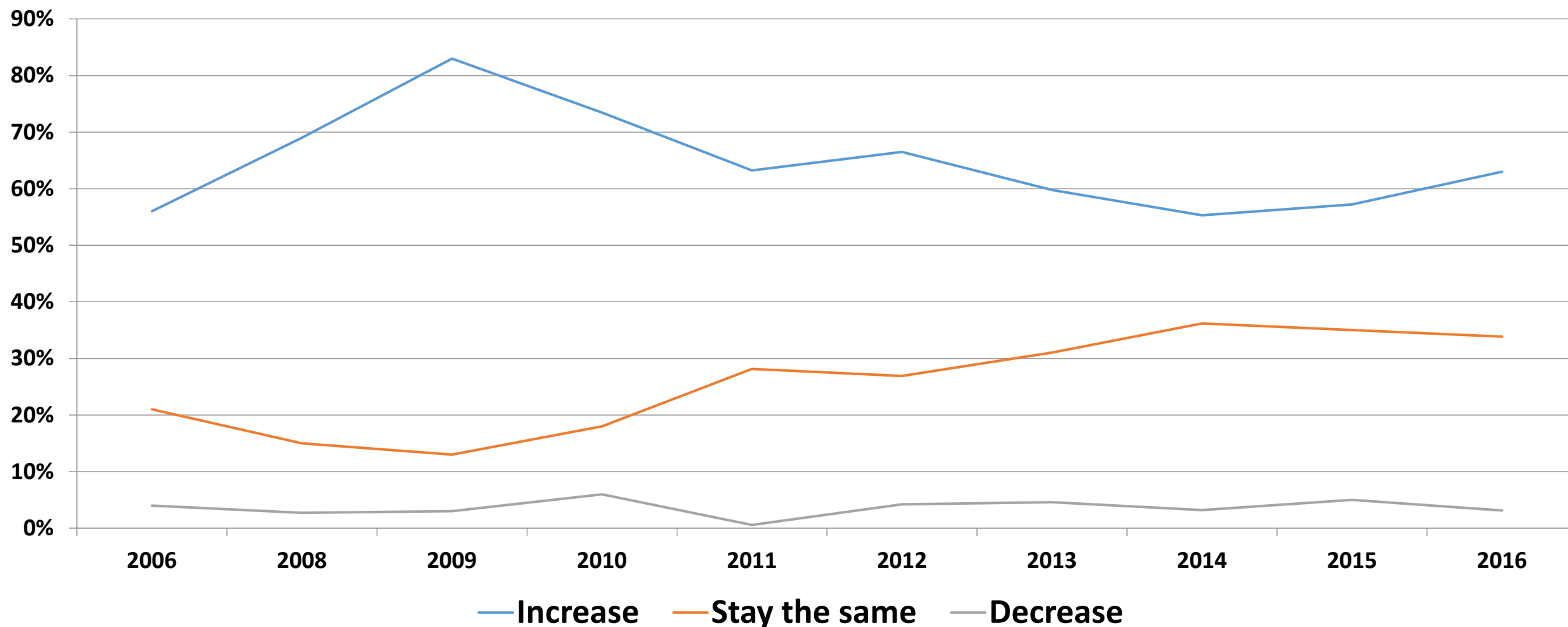
Satisfaction rates with ETFs



Among users of ETF for the respective asset class

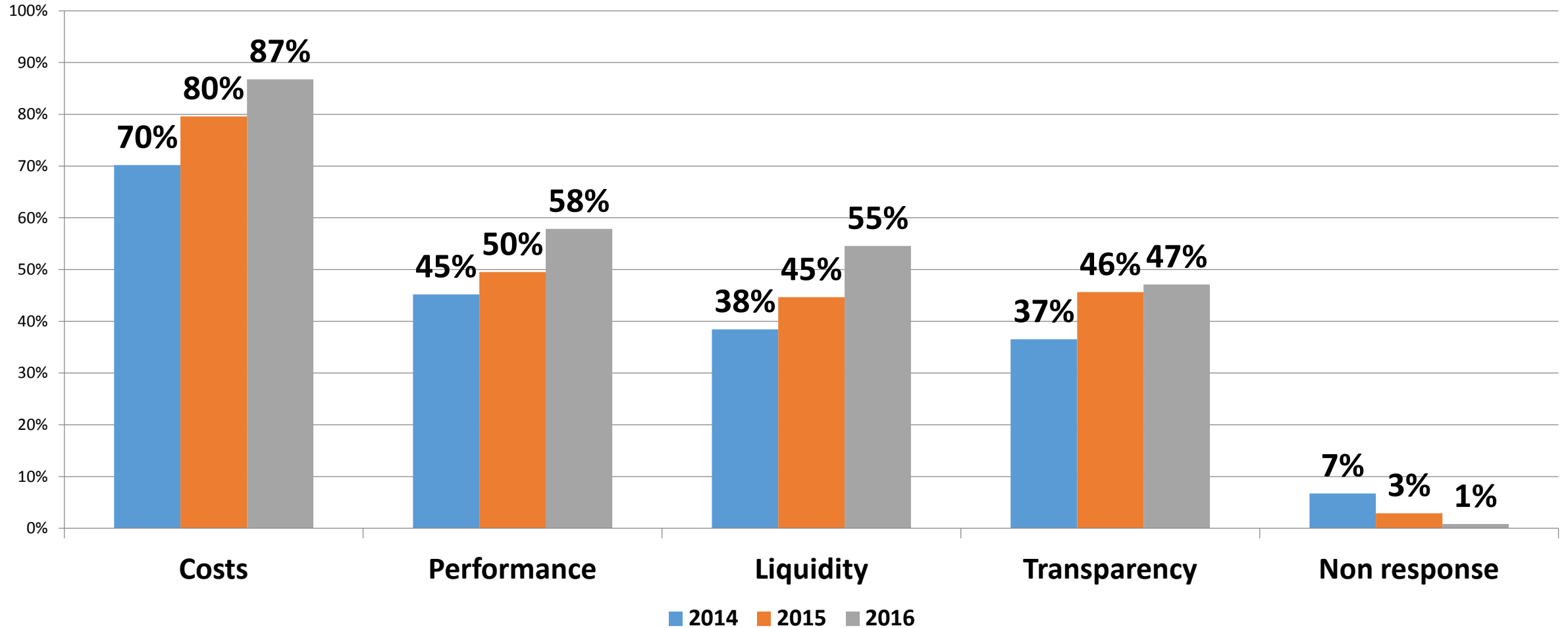
- High satisfaction with ETFs in traditional asset classes
- More reserved about ETFs for alternative asset classes

Positive outlook on future use of ETFs



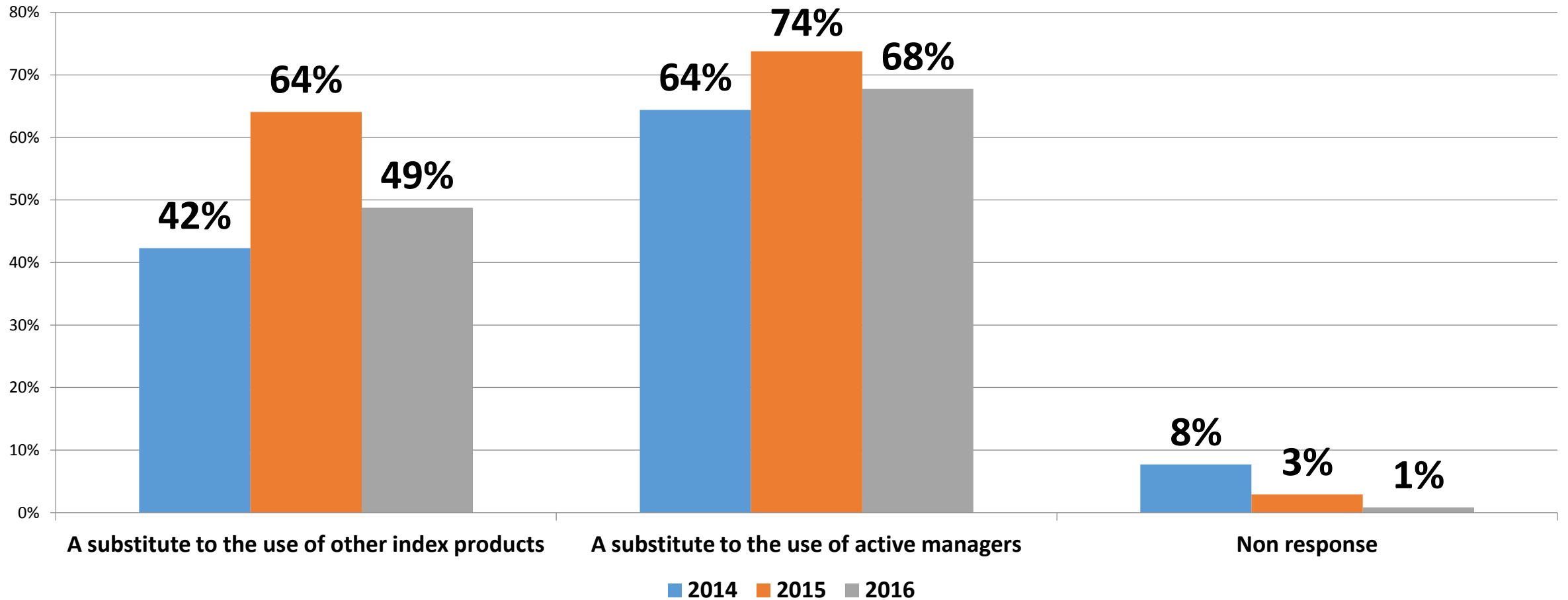
- In 2016, 63% of respondents plan to increase their use of ETFs; 3% plan to decrease it.

Motivations for increasing the use of ETFs



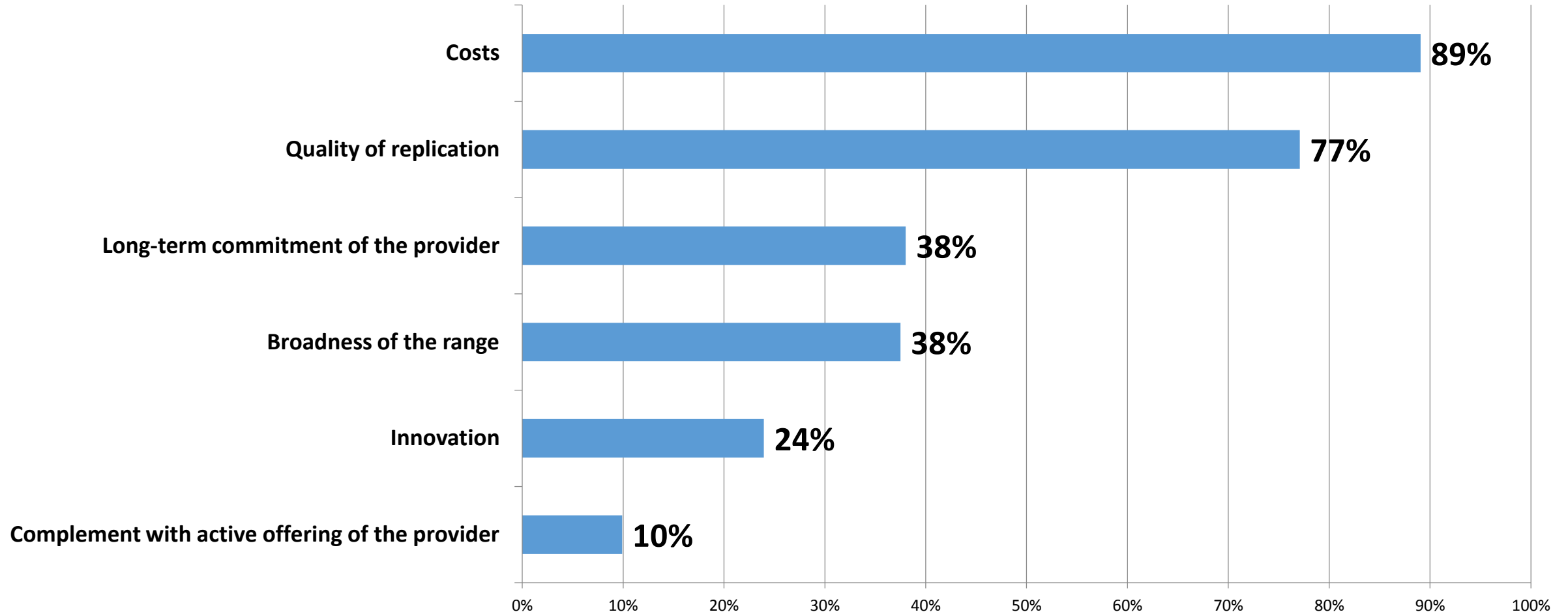
- Lowering costs in the main motivation for future adoption of ETFs.

ETFs as a substitute for active and passive management



- Increasing the use of ETFs will serve not only to replace active managers, but also to replace other passive investing products.

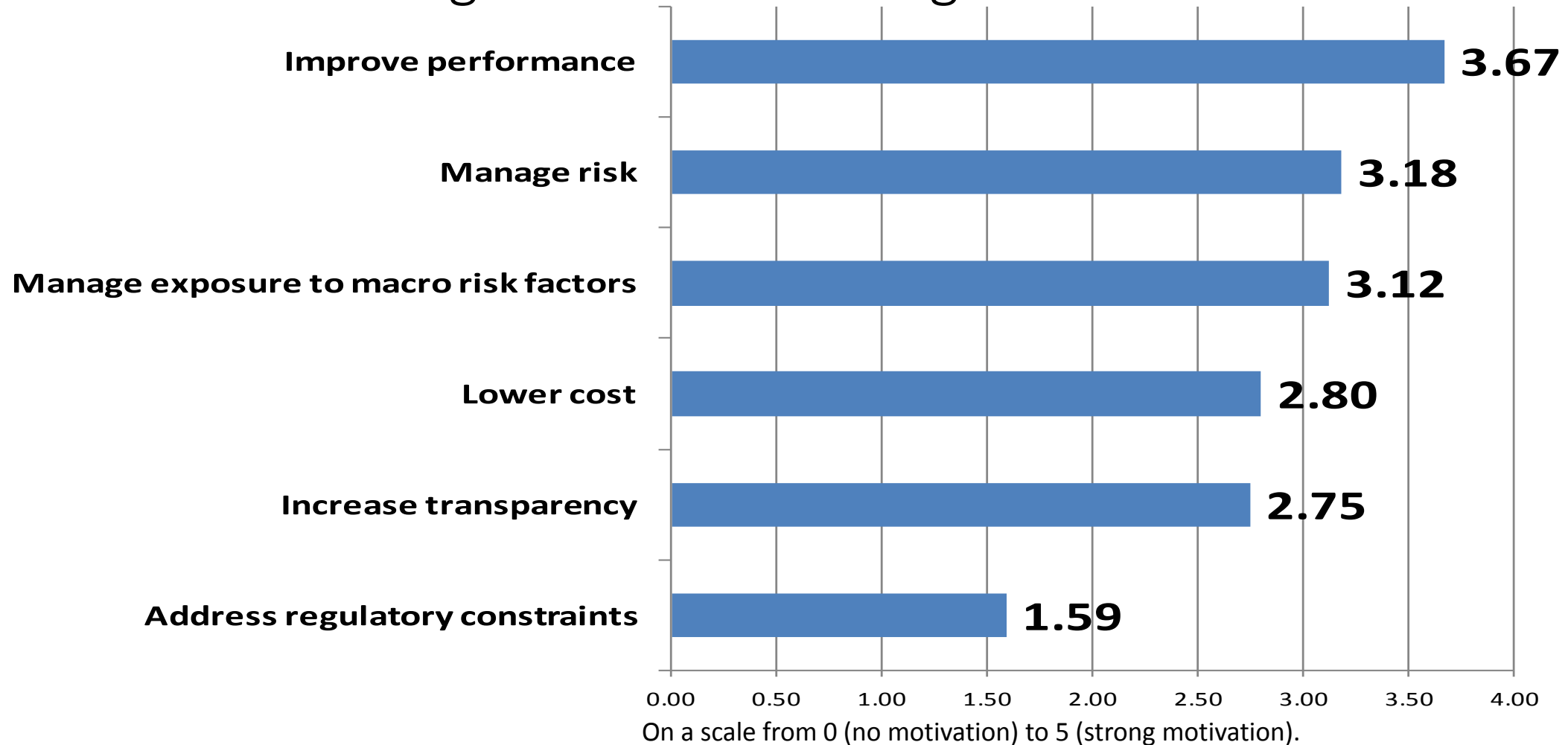
Criteria for selecting ETFs



- Costs and quality of replication are the main criteria to select ETFs.

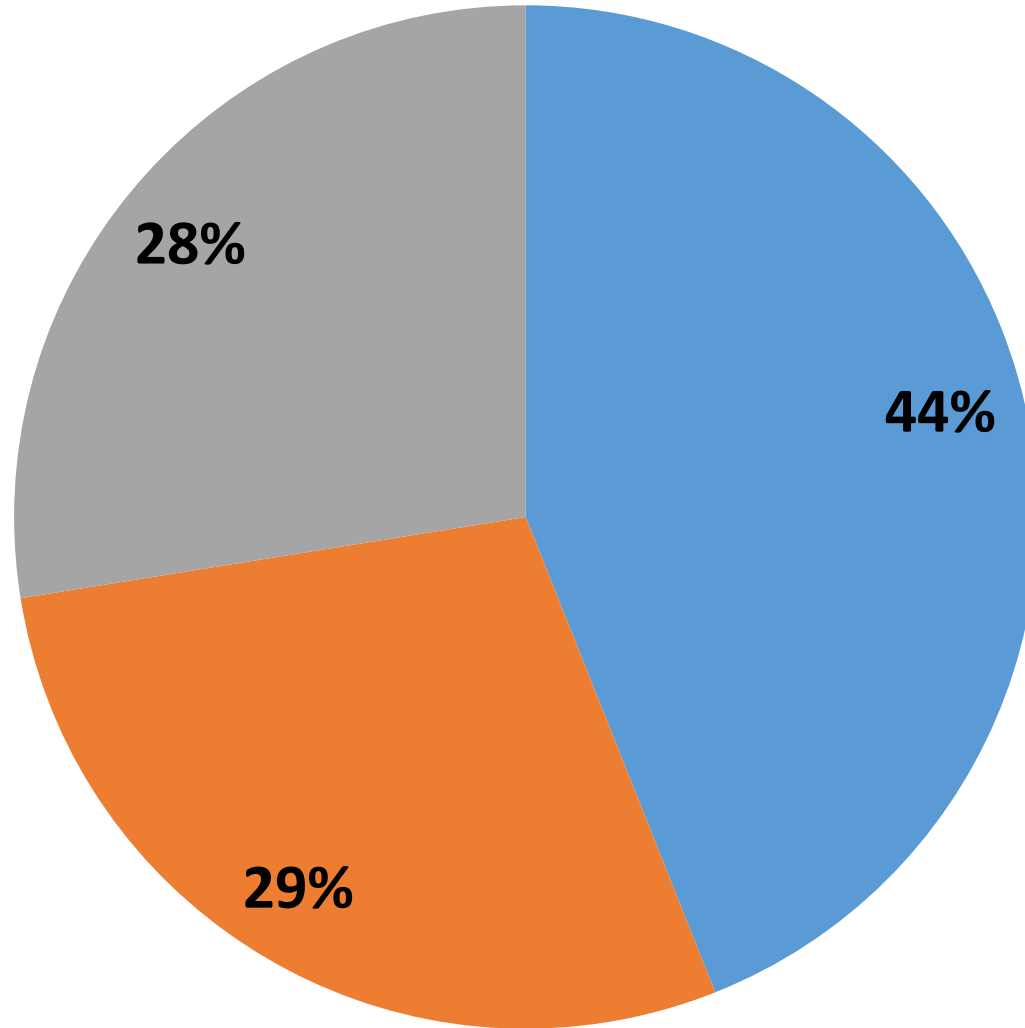
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Motivations for using smart beta strategies



- The quest for outperformance is the main driver for smart beta strategies.

Current use of smart beta strategies

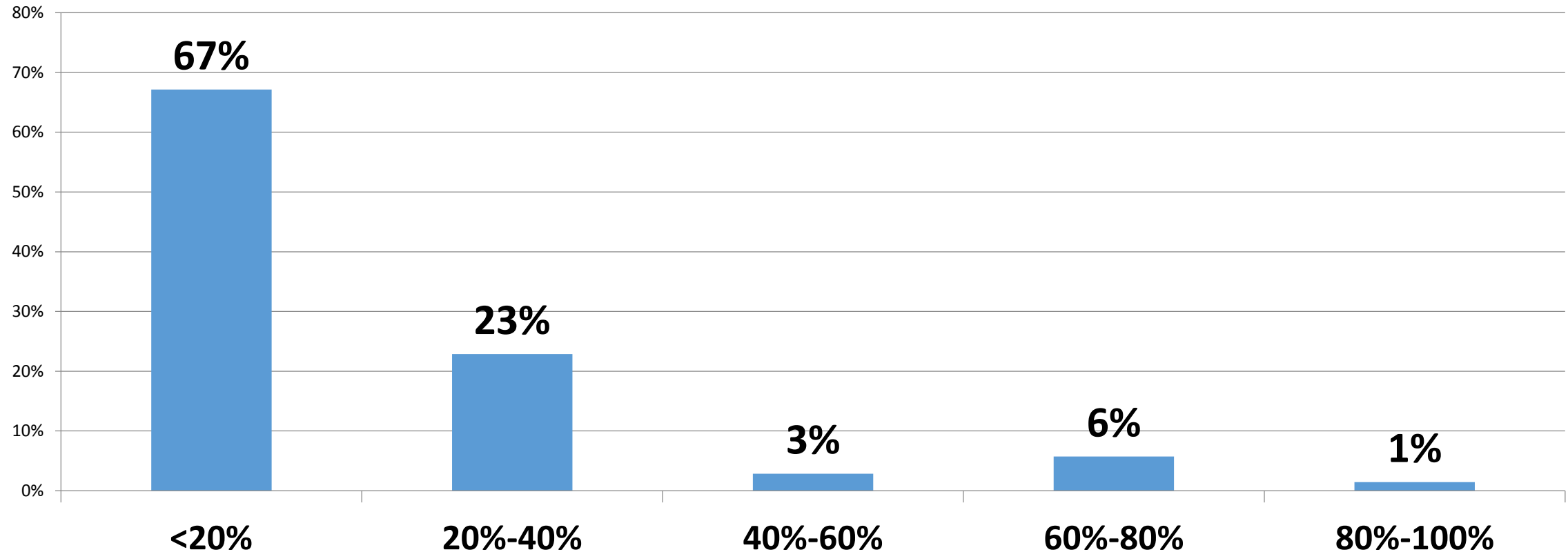


■ My organisation is investing in such products

■ My organisation is considering investment in such products in the near future

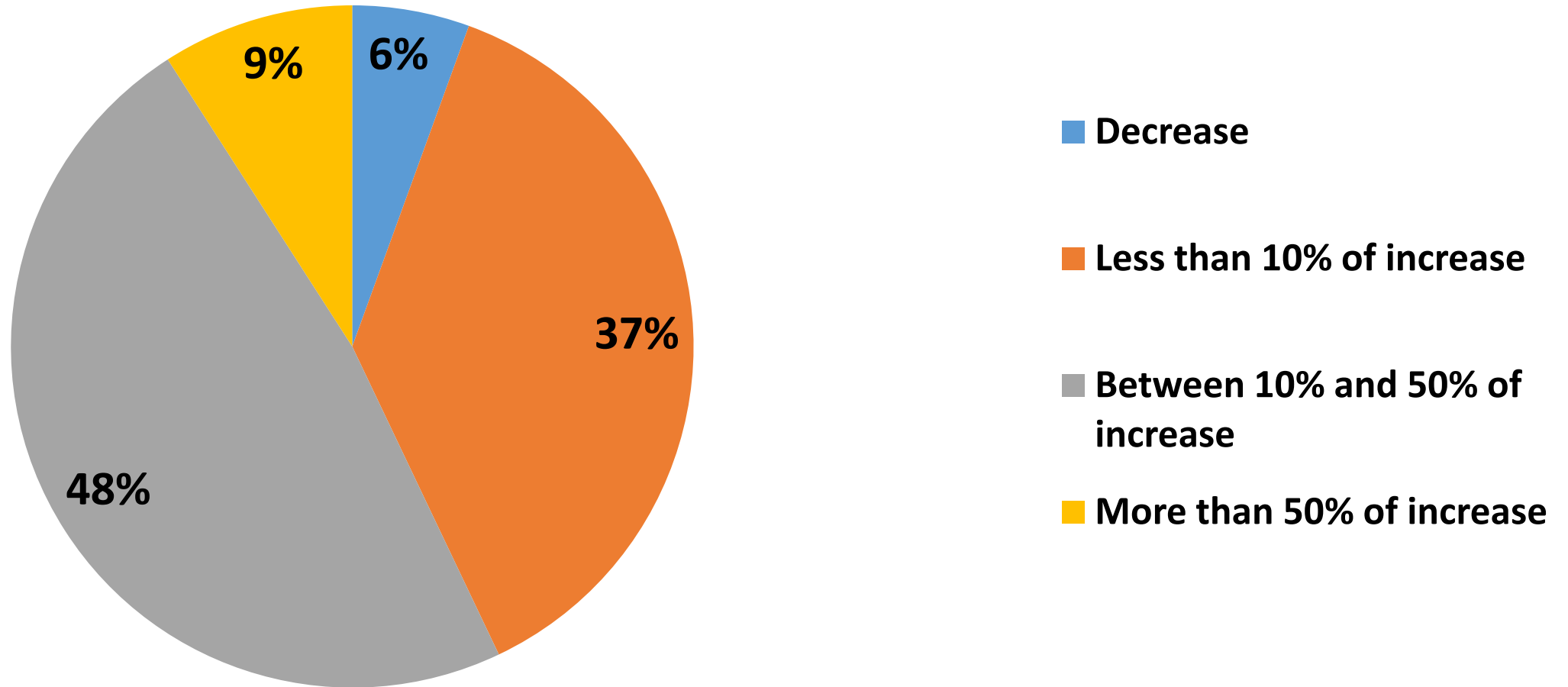
■ My organisation is not investing and not considering investment in such products in the near future

Early stage of implementation (I)



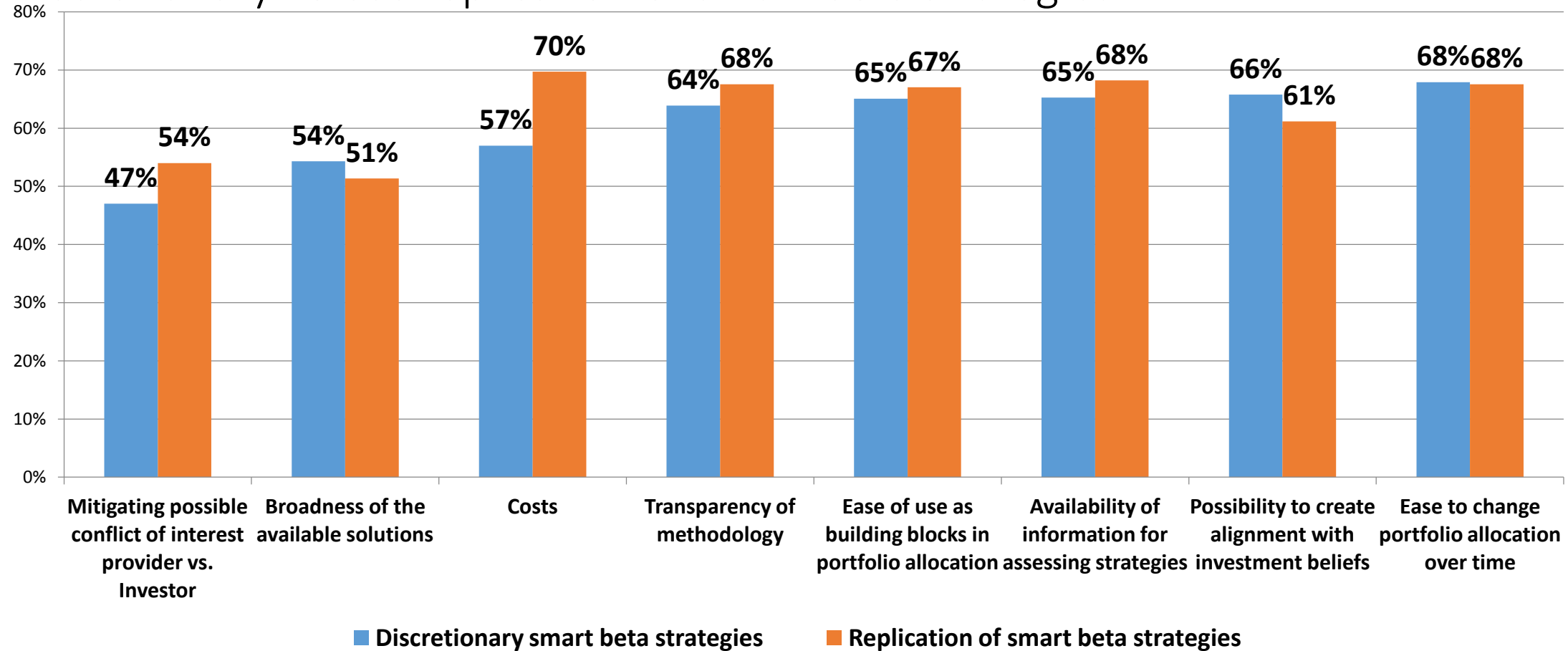
- Two-thirds of respondents invest less than 20% in smart beta strategies.
- Only 10% invest more than 40% of their total investment in smart beta strategies.

Early stage of implementation (II)



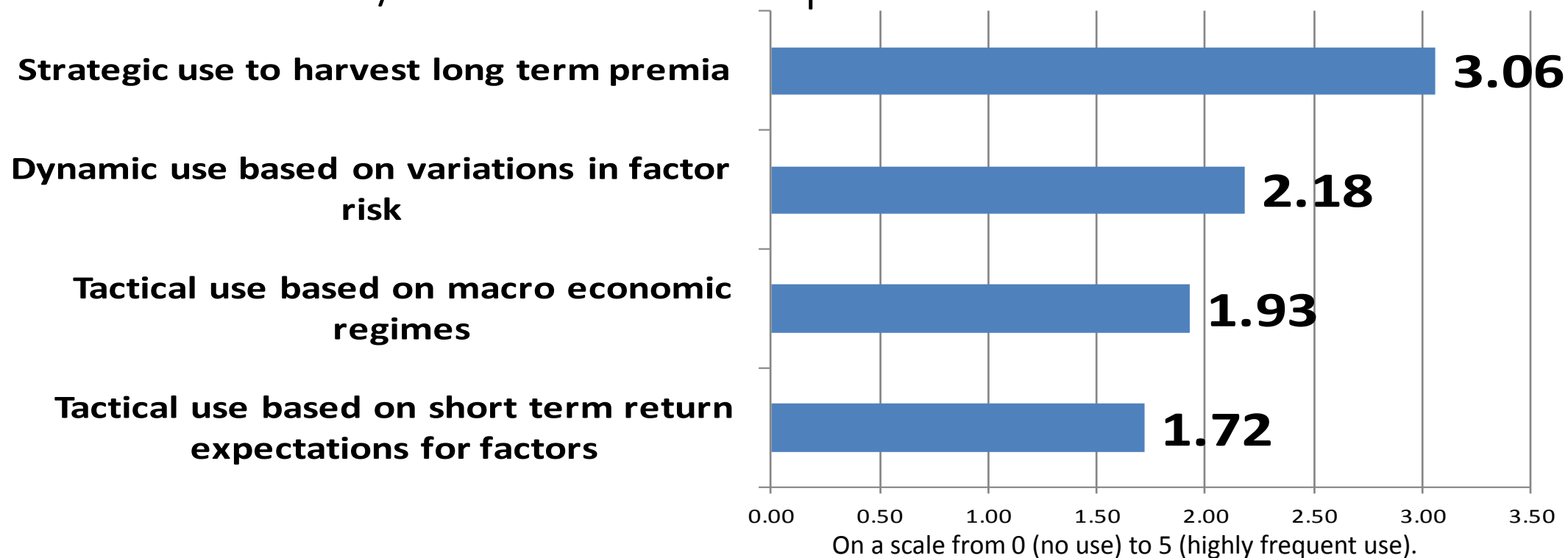
- 57% of respondents plan an increase of more than 10% of their smart beta investment in terms of assets over the near future. Only 6% plan a decrease.

Discretionary versus replication of smart beta strategies



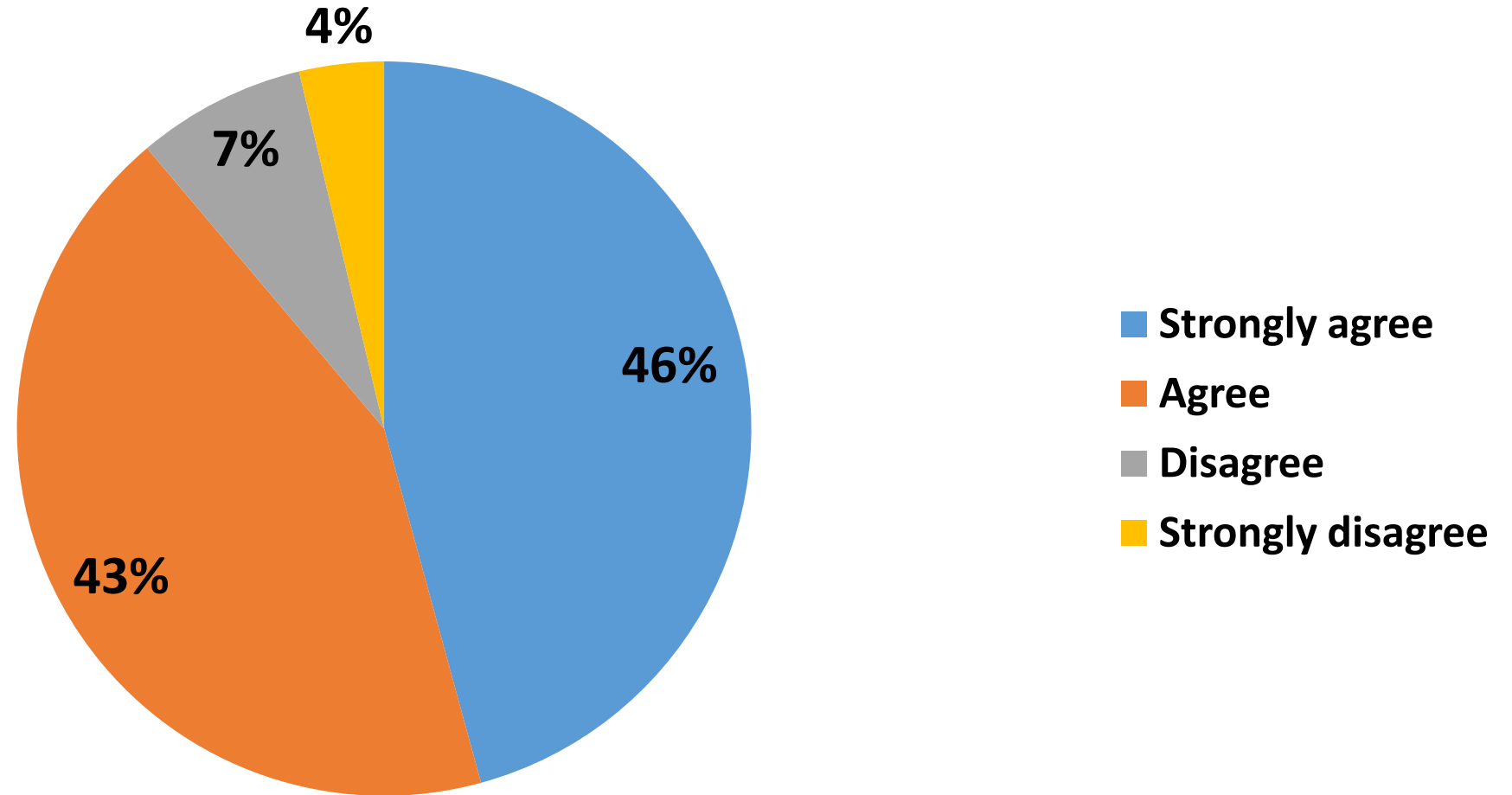
- The biggest advantage of replicating indices is costs.
- Slight advantage of discretionary smart beta strategies in terms of breadth of available products and for the possibility to account for specific investment beliefs.

Use of smart beta / factor-based exposure



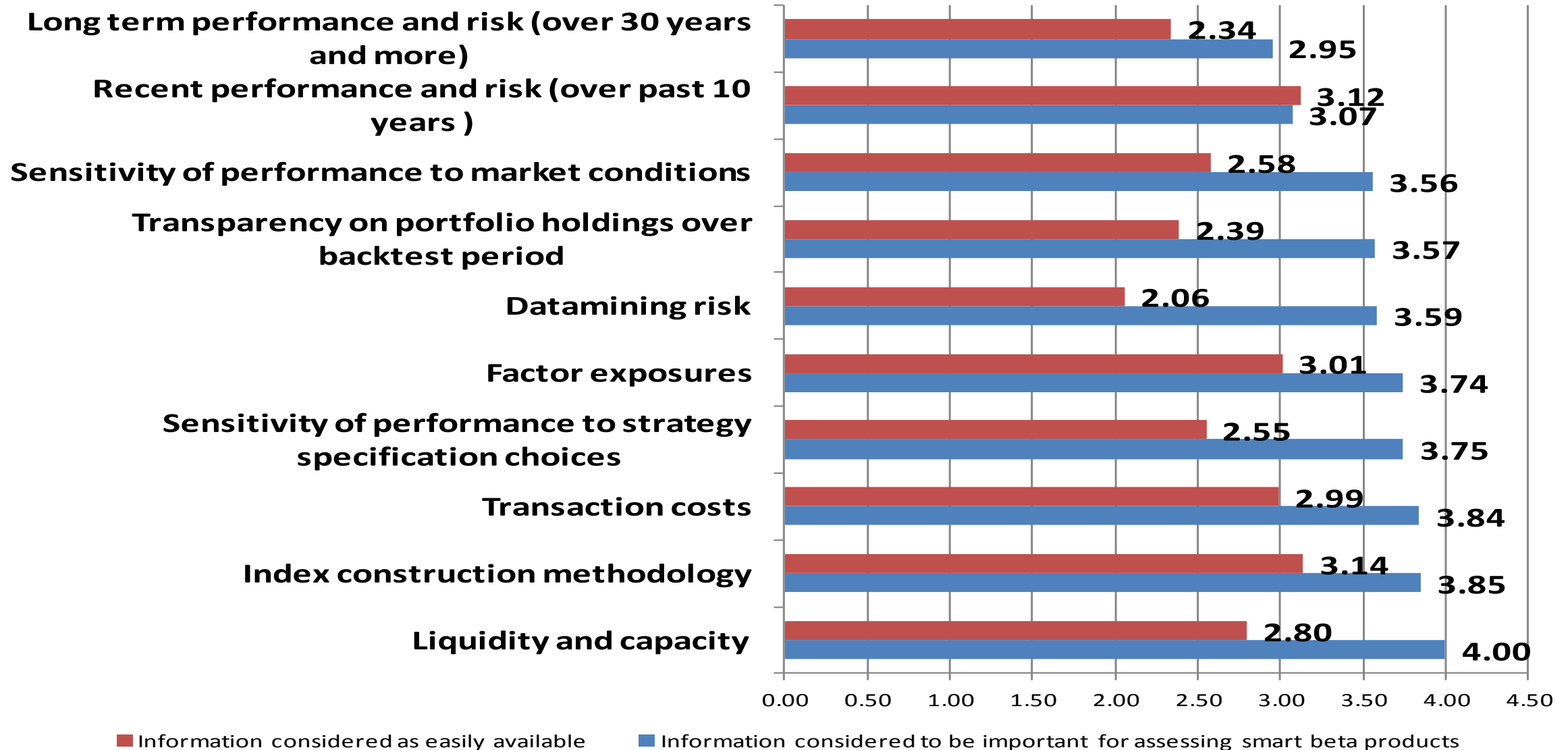
- The most frequent use is a strategic use to harvest long term premia.
- The least frequent use is a tactical use based on short term return expectations for factors.

Information about smart beta strategies



- 89% of respondents declare that smart beta indices require full transparency on methodology and risk analytics

Information regarded as important is not considered to be easily available

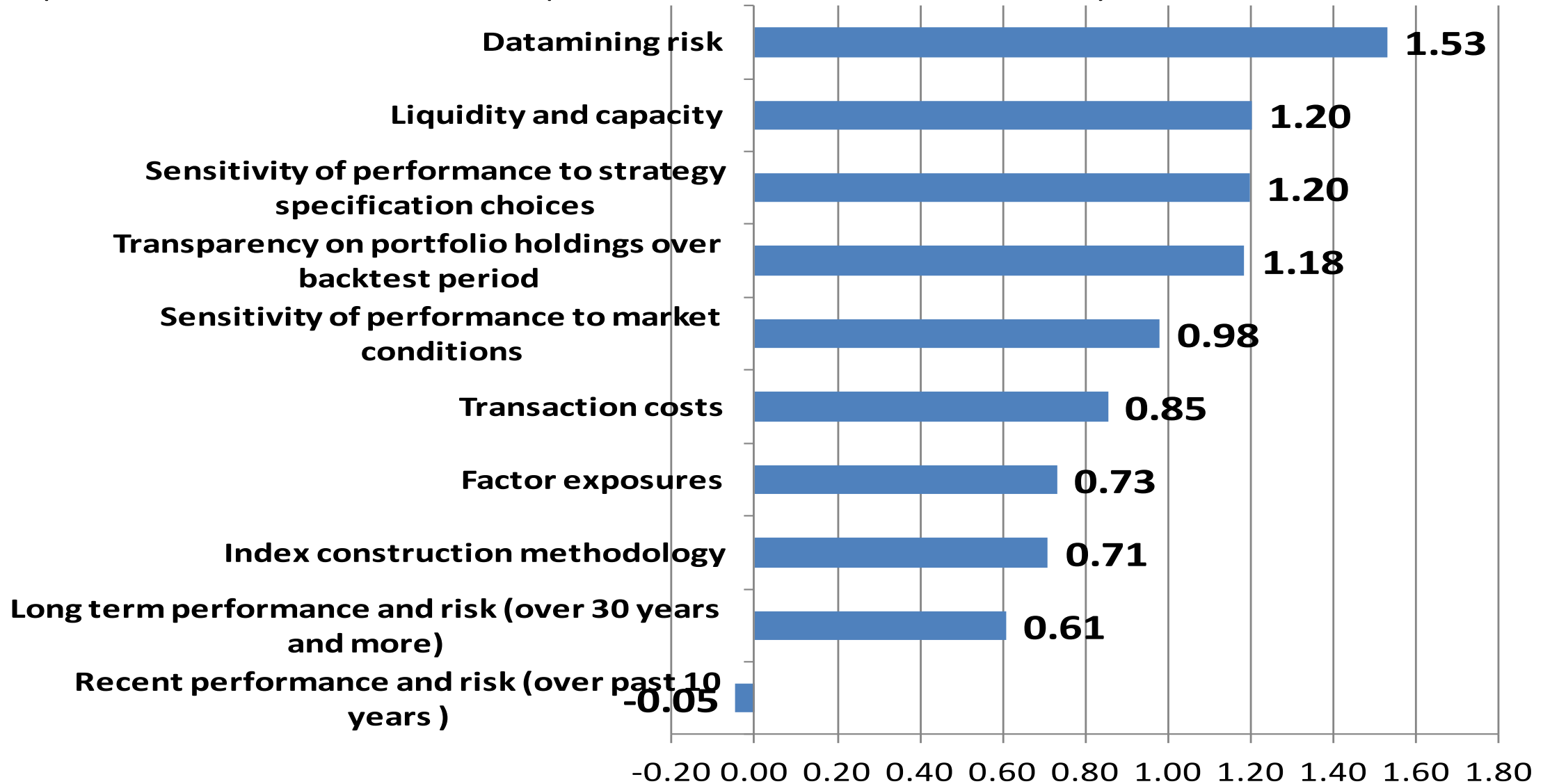


On a scale from 0 (difficult to obtain) to 5 (easy to obtain) and on a scale from 0 (not important) to 5 (crucial), respectively.



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Gap between investors' requirements and accessibility of information

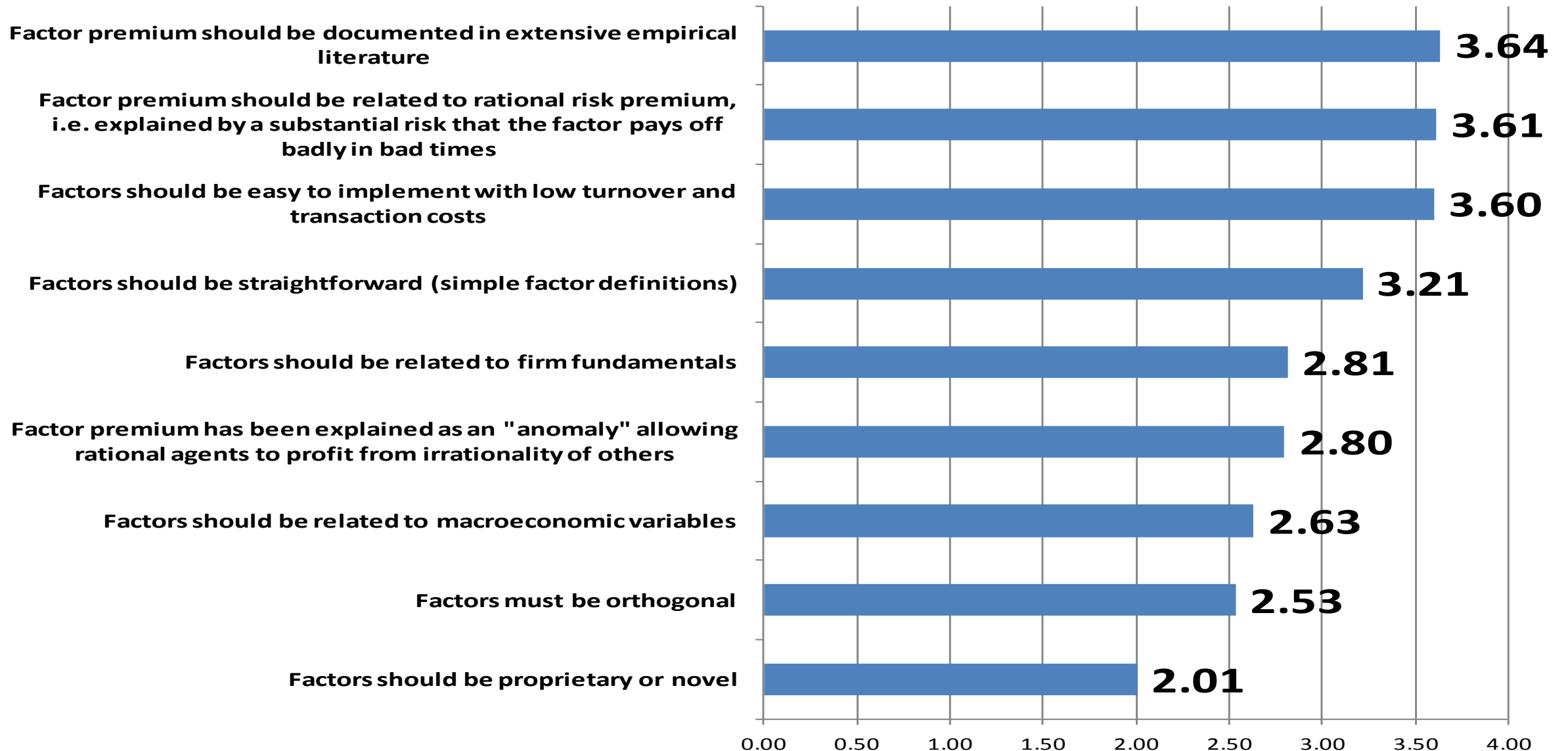


The gap is computed as the difference between the score of information importance and the score of information accessibility.



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Requirements for factors



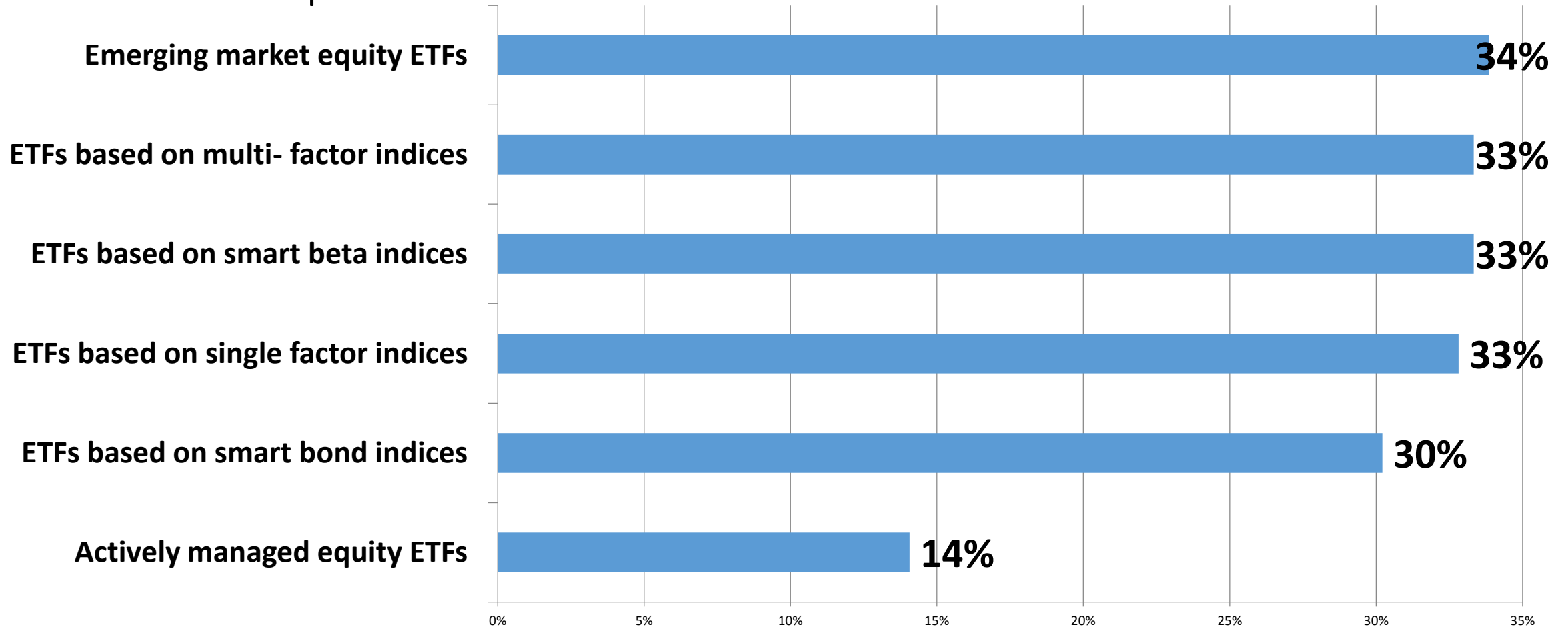
On a scale from 0 (not important) to 5 (absolutely crucial).



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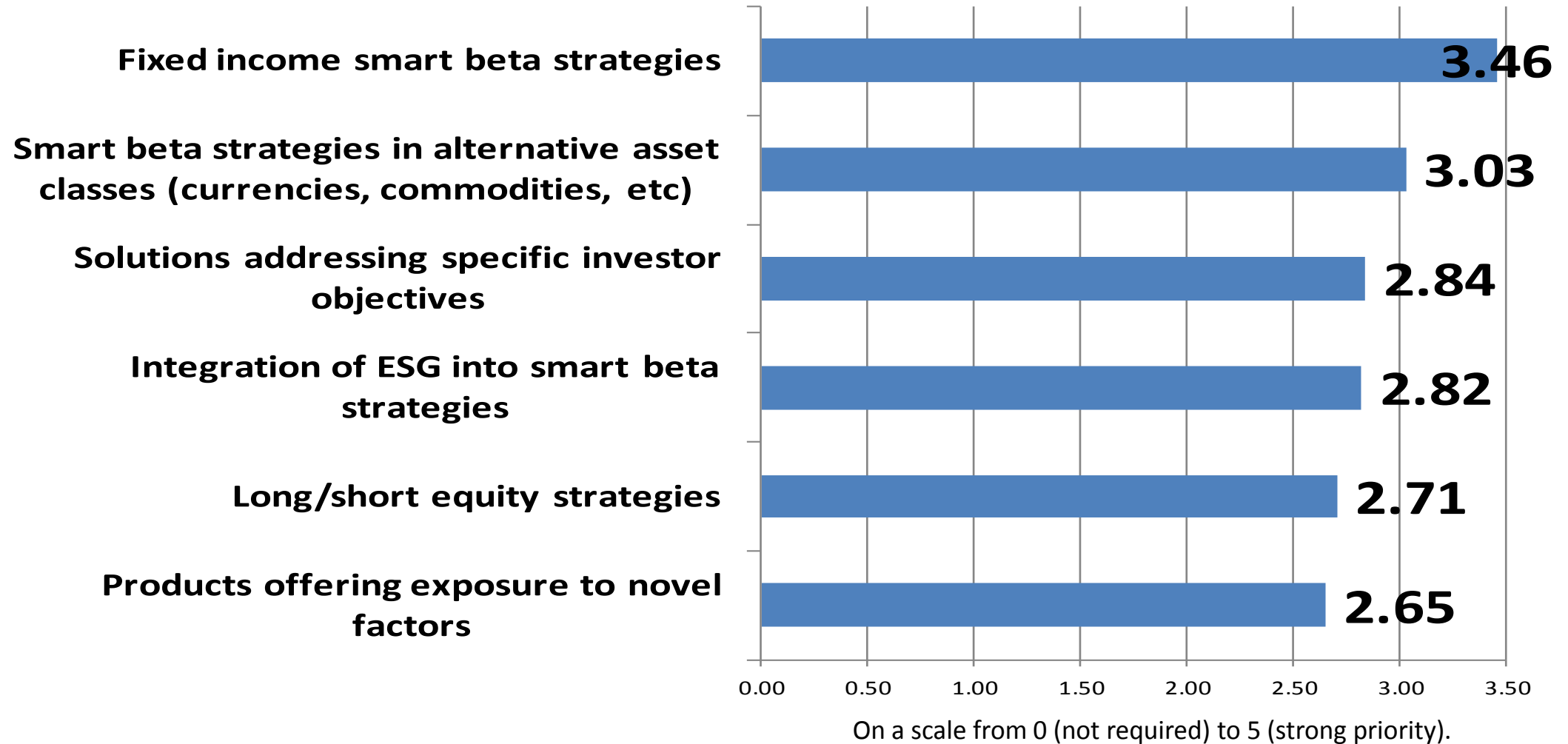
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Future developments for ETFs



- 54% of respondents want further developments in at least one of the three categories of advanced forms of equity indices (single factor, multi-factor, smart beta).

Future developments for smart beta strategies



- Further developments are mainly required in the area of fixed income and alternatives.

References

- EFAMA. 2017. Challenges ahead for the European Fund Industry.
- ETFGI. 2016. ETFGI monthly newsletter December 2016. Available at www.etfgi.com.
- Lyxor ETF Research. 2017. European Smart Beta ETF Market Trends. Q4 2016 in brief.