

ETF INSIDER

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Beware Nvidia dominance

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for investors

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Thematic ETFs out of favour

Welcome to the April edition of *ETF Insider*, the first ETF magazine dedicated to professional investors across Europe. Each month, we produce analysis on a specific area of the market, be that fixed income, emerging markets or factors while also providing expert insights into the latest on asset allocation and portfolio construction, always through an ETF lens.

This issue focuses on thematic ETFs, a segment of the market that has suffered a lull in demand over the past 18 months since Russia's war in Ukraine and the resulting inflation that sent shockwaves across global markets. Thematic ETFs, which tend to offer exposure to growthier segments of equities, are yet to see a pick-up in flows despite current bullish sentiment.

According to data from ETFbook, thematic ETFs have seen \$116m outflows so far in 2024, as at 22 March, adding to the \$1.1bn net redemptions seen last year versus a combined \$16.3bn inflows in 2021 and 2022. Assets in thematic ETFs currently total \$44bn, as at the end of 2023.

With Nvidia driving over a third of the returns for many thematic ETFs, there is reason for fund selectors to be cautious. The chipmaker's surge is

testing the limits of the UCITS 20/35 rule, with concentration risk not just an issue for broad-based benchmarks (p.36). How thematic ETF issuers balance theme purity, diversification and liquidity is a timely topic as a total focus on the purity of the megatrend can lead to construction problems if there are significant inflows into the strategy (p.24).

Elsewhere, Parala Capital's Steven Goldin takes a deep dive into low volatility UCITS ETFs and the unique business cycle sensitivities fund selectors need to be aware of (p.30), while two ETF Buyers Club members INVICO Asset Management's Bruno Schneller and IDAD Funds' Andy Merricks evaluate the opportunities in biotech (p.16) and the role of thematic ETFs within portfolios (p.18), respectively.

Finally, keep an eye out for the usual segments 'Education Corner' (p.12), 'ETF of the month' (p.13) and 'Fund Fights', where *ETF Stream* compares the strengths and weaknesses of similar ETFs (p.14). Finally, I want to highlight our Expert Investors series where *ETF Stream* interviews fund selectors about their asset allocation and ETF usage (p.11).

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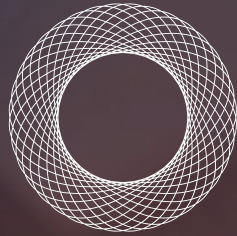
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News & views

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Thematic ETFs: Timing is everything

Avoid the latest fads and adopt a long-term time horizon

By Tom Eckett

First it was clean energy then artificial intelligence. Thematic ETFs offer exposure to structural long-term megatrends, however, timing the entry point is just as important as selecting the right theme.

BlackRock's clean energy ETF provides a perfect example of this. While the iShares Global Clean Energy UCITS ETF (INRG) returned 17.6% annualised over the five years to end of June 2023, the annualised return for investors – based on inflows and outflows – was -5.5%, a 23 percentage point (ppt) gap, according to Morningstar research. This is an extreme example given the thematic ETF poster child saw \$5.8bn inflows between November 2020 and January 2021, however, it highlights

the challenge of not only selecting the right ETF but also choosing when to invest.

“Investor buying and selling habits connected with thematic funds over the last five years have destroyed considerable value,” Kenneth Lamont, senior fund analyst at Morningstar, warned. “Fund investors are collectively poor market-timers and they particularly struggle in more volatile and exotic funds compared with more diversified core building blocks.”

This is especially pronounced for thematic ETFs which have more concentrated portfolios. In the search to offer the purest exposure to a particular megatrend, ETF issuers move down the market-cap spectrum, potentially leading to greater volatility. “ETFs’ concentration

results in high levels of volatility,” Lamont added. “More volatile funds seem to induce more frequent trading and a tendency to buy high and sell low. Most investors would achieve better investment outcomes by adopting a more patient buy-and-hold approach.”

As a result, demand for thematic ETFs has waned, with some investors concerned about the volatility and overlap with traditional sectors.

According to data from ETFbook, thematic ETFs have seen \$116m outflows so far in 2024, as at 22 March, adding to the \$1.1bn net redemptions seen last year.

This is in stark contrast to the combined \$16.3bn inflows seen in 2021 and 2022 as investors rode the wave of the digital shift following the COVID-19 pandemic. Assets in thematic ETFs currently total \$44bn, as at the end of 2023.

How thematic ETFs fit within a multi-asset portfolio is a challenge for fund selectors, with questions around whether they remain a satellite holding or can be incorporated as a core building block.

“Thematic ETFs will likely always be used as an extension to allocations in more traditional sectors, and normally only in higher risk portfolios, as opposed to being standalone allocations within our strategic asset allocation,” Terry McGivern, senior research analyst at AJ Bell, told *ETF Stream*.

“This is because there is often a high degree of overlap with traditional sector/regional exposures and also because many of the newer themes do not have the data available to really work them into a normal capital market assumptions and asset allocation framework.”

Final word

Thematic ETFs can be a fantastic way to add alpha to portfolios, however, in a market where the number of products is booming, selecting the right ETF and adopting a long-term time horizon has never been more vital.

“More volatile funds seem to induce more frequent trading and a tendency to buy high and sell low. Most investors would achieve better investment outcomes by adopting a more patient buy-and-hold approach.”

Tom Eckett is editor of ETF Stream

Dateline: The month in review

4 March

French government paves way for first active ETF listings on Euronext Paris



The French government has announced a regulatory change to allow the listing of active ETFs on Euronext Paris for the first time. In a decree published by the Prime Minister on 27 February, the government said it would remove the conditions under its monetary and finance code which had previously prevented their listing. This change is expected to modernise the savings product range and enhance the Paris market's competitiveness. The move is well placed amid the European active market's strong growth, with \$32.9bn assets under management (AUM) at the end of 2023, according to data from ETFbook.

8 March

ARK Invest Europe to launch three active ETFs in April



Cathie Wood's ARK Invest Europe is set to launch three new active ETFs in April, including the flagship ARK Innovation ETF (ARKK), expanding its presence in the European market following its acquisition

11 March

Crypto ETNs to list on London Stock Exchange following FCA decision

The London Stock Exchange will start accepting bitcoin and ethereum ETN applications for professional investors in Q2 after the Financial Conduct Authority (FCA) said it will 'not object' to requests to list crypto ETNs on regulated exchanges. To list on the exchange, crypto ETNs must be physically backed, non-leveraged and offer exposure to bitcoin or ethereum only. The 2020 ban on retail investors accessing the products also remains in place.



of Rize ETF in September last year. The launches are part of ARK's strategy to introduce familiar active management approaches from the US to Europe, with ARKK alone growing from \$6.5bn to \$7.5bn assets due to market gains. Additionally, ARK plans to continue developing new product lines and will maintain the Rize ETF brand as a "sustainable sub-brand" for further product development.

11 March

DWS's global capital markets head Shastry to depart

Keshava Shastry, global head of capital markets at DWS, will leave the firm after more than a decade of service. Shastry – who joined DWS from Credit Suisse Asset Management in November 2013 – will be replaced by DWS's European head of capital markets Jamie Hartley, an industry source told *ETF Stream*. Shastry is also chair of the Investment Association's ETF committee and chair of the European Fund and Asset Management Association's ETF task force.

13 March

ETF industry rallies against progressive cash penalties under CSDR

European investment groups are uniting against proposed progressive cash penalties for ETFs under the Central Securities Depository Regime (CSDR), arguing it could hurt the region's competitiveness. If introduced, penalty rates would rise from 2.5 basis points (bps) on day one to 12.5bps if ETFs fail to settle six days after the intended settlement date. Critics – including the Association of Financial Markets Europe and Jane Street – warn that higher penalty rates for settlement fails could increase trading costs and make EU ETFs less appealing to investors by forcing wider bid-ask spreads.

14 March

Amundi launches Europe's cheapest all-world ETF

Amundi has unveiled the continent's most competitively priced ETF that

spans developed and emerging markets, boasting fees of less than half of its closest competitor. The Amundi Prime All Country World UCITS ETF (WEBG) listed on Deutsche Boerse with a total expense ratio (TER) 0.07%. The ETF offers broad exposure to 3,469 large and mid-cap companies across both developed and emerging markets. Invesco's and State Street's competing products have fees of 0.15% and 0.17%, respectively.

14 March

DWS launches Europe's first world ex-US ETF



DWS unveiled Europe's first MSCI World ex-US ETF, aiming to offer investors a way to diversify by specifically excluding US equity allocations. The Xtrackers MSCI World ex USA UCITS ETF (EXUS) listed on the Deutsche Boerse and the London Stock Exchange (LSE) with a total expense ratio (TER) of 0.15%. EXUS tracks the MSCI World ex USA index, featuring 870 companies across 22 developed markets, with Japan, the UK, and France as its top exposures. This move allows investors to adjust their US equity exposure more precisely, responding to the growing dominance of US equities in global portfolios.

18 March

BlackRock launches synthetic global ETF

BlackRock expanded its synthetic range with the launch of a global equity ETF. The iShares MSCI World Swap UCITS ETF (IWDS) listed on Euronext Amsterdam with a total expense ratio (TER) of 0.20%. The ETF tracks the MSCI

World Net TR index, covering 1,480 equities across 23 developed countries, using an unfunded swap model for improved tax efficiency on US equities. The ETFs do not pay withholding tax on dividends – as the substitute basket of the ETF is restricted to non-dividend paying stocks – meaning it delivers a lower annual tracking difference versus its physical counterparts.

18 March

Bond ETF inflows slow amid changing rate expectations

Bond ETF inflows significantly slowed last month, marking the weakest month of asset gathering “in years” for fixed income UCITS ETFs as investor expectations shifted away from steep interest rate cuts in 2024. BlackRock experienced notably low inflows into its European ETFs with just over €1bn collected which marked its smallest monthly increase in nearly two years, driven by a reassessment of future rate cuts amid higher-than-expected US inflation.

20 March

Hedge funds look to launch ETFs amid active boom

Amid the active ETF boom, there is an increasing appetite among hedge funds to enter the ETF market with their own strategies, according to white-label ETF issuers. The expansion of the active ETF market in Europe, allowing for daily liquidity as opposed to the traditional monthly liquidity of hedge funds is a key driver of this trend, with Lisa Mantil, global head of Goldman Sachs ETF Accelerator, citing an “opportunity cost” of clients not being in the space. Waystone ETFs and HANetf reported increased demand from hedge fund managers to adapt their strategies into a UCITS ETF format, detailing the advantages such as transparency and tradability.

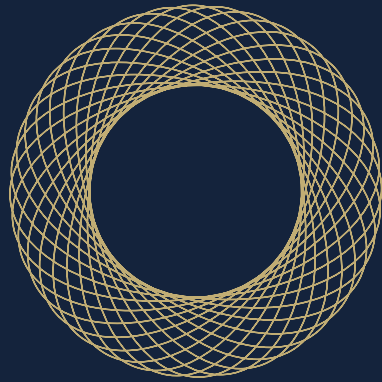
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ETFs key for tactical allocations in government bonds

Expert Investors is a series where ETF Stream interviews fund selectors on the role of ETFs within their asset allocation. In the hot seat this month is Chris Forgan of Fidelity



“You can either look to capture that shorter term opportunity set through futures, ETFs or index funds. We incorporate ETFs for shorter-term tactical opportunities.”

On the equity side, Forgan noted the US remains his team’s “key overweight” but defensive elements of the market – such as healthcare staples and utilities – are “looking cheap”.

Not using active ETFs

Interestingly, despite Fidelity being the third-largest issuer of actively managed UCITS ETFs – with an 11.1% market share at the end of 2023 – Forgan said his team currently does not use the structure but believes active management represents “an interesting opportunity set” for ETFs.

“It is an approach which has been more commonly used in the US,” he continued. “In Europe, we are behind in terms of the evolution of the ETF product cycle, but it offers an interesting way in which you can bring actively managed strategies to the market in a wrapper that may be more suited to certain end investors.”

Investor evolution

Moving away from products, Forgan argued further development is needed in accessing ETFs and education on the wrapper. “From surveying clients, ETFs are still not easily accessed yet and that is another opportunity for ETF providers to make these products more readily available through platforms for retail investors, ultimately. That would allow for greater adoption more broadly.”

He added clients’ natural reaction to passive products is to compare headline fees and greater understanding of total cost of ownership is needed.

“There is still education that needs to be done to move people away from what is still a focus on the headline rate, which does not capture everything.

“Other considerations such as jurisdiction and replication methodology are necessary when evaluating ETFs and which one offers the best outcome.”

By **Jamie Gordon**

With divergent monetary policy cycles back in focus across developed and emerging markets, Chris Forgan, portfolio manager, multi-asset, at Fidelity International, has said ETFs offer a “nimble” and “cost-effective” tool to capture sometimes hard-to-access exposures in the sovereign debt space.

A key example of this, Forgan said, was when his team looked to tap Chinese government bonds at relatively attractive yields, although Sino sovereigns had “historically not been the easiest thing to access”.

“In Europe, we are behind in terms of the evolution of the ETF product cycle, but it offers an interesting way in which you can bring actively managed strategies to the market in a wrapper that may be more suited to certain end investors.”

“That was something we had in the portfolio a year or so ago and the only way to get that was through an ETF vehicle,” Forgan added. “There was not much choice in the market at that particular point in time. The ETF gave us that exposure in a cost-effective manner and the scale of the product gave us that nimbleness to be able to enter and exit with no meaningful cost risk attached.”

Looking ahead, Forgan said UK gilts and German bunds look “quite interesting” for those trying to capture areas of the global economy where this is some support to the inflation story and where there has been “meaningful repricing of risk” over the past 18 to 24 months.

Jamie Gordon is senior features reporter at ETF Stream

CSDR and its impact on ETFs

Cash penalties do little to reduce settlement failures

The Central Securities Depositories Regulation (CSDR) was introduced by the European Parliament and Council in 2014 to harmonise settlement standards and improve settlement efficiency across the region.

The regime aims to provide a common set of requirements for central securities depositories (CSDs) operating across Europe in the aftermath of the Global Financial Crisis (GFC) in 2008.

CSDR requirements have been implemented across three phases:

- **Phase 1:** In 2017, firms were required to offer the option between omnibus and individual aggregated accounts
- **Phase 2:** In 2019, firms were required to report internally settled trades

Following two delays from the European Commission, Phase 3 of CSDR – known as the Settlement Discipline Regime (SDR) – came into effect on 1 February 2022.

SDR introduced a set of requirements to address settlement fails including cash penalties and mandatory buy-ins, although the latter was delayed by ESMA for three years amid market warnings it could lead to increased costs and reduced liquidity across asset classes.



Through the implementation of cash penalties, the regulator was hoping to deter participants from settlement fails and ensure they settle trades in a timely manner. However, the European ETF market, in particular, has been grappling with the challenges posed by CSDR.

Despite the threat of fines, European ETFs have experienced an increase in settlement failures since the introduction of Phase 3 of CSDR with one in 10

“The regulator was hoping to deter participants from settlement fails and ensure they settle trades in a timely manner.”

transactions needing correcting or failing, according to data from SWIFT. This is largely because many ETFs offer exposure to underlying securities from several jurisdictions, especially global and regional equity strategies.

As a result, authorised participants (APs) appear happy to face severe penalties for settlement failures which they are passing on to investors via wider spreads, especially when compared to the costs of an ETF creation.

The situation could become even more acute if Europe follows the US in moving from a T+2 to a T+1 settlement regime, an issue that could drive a further increase in the number of settlement failures across the continent.

“Because settlement of newly created units is contingent on the settlement of the underlying constituents, this can often lead to settlement delays in a T+2 environment, due to time zone differences, market holidays and cross-border settlement complexity,” the Association for Financial Markets in Europe (AFME) said. “These challenges would be even more pronounced in a T+1 environment.”

The question now is whether the regulator will view mandatory buy-ins, a process that contractually requires APs to source securities elsewhere in the event of a settlement fail, as the solution to the poor settlement rates. This part of CSDR is an area market participants continue to be firmly against.





STAT ATTACK	
Ticker	EXSE
Launch date	04/04/05
AUM	\$914m
TER	0.20%
Constituent count	200
Data as at 27 March	

iShares STOXX Europe Small 200 UCITS ETF (EXSE)

This issue’s ETF of the month is BlackRock’s EXSE, which booked impressive inflows as the ECB struck a dovish tone in its March policy meeting

This issue’s ETF of the month is BlackRock’s EXSE, which booked impressive inflows as the ECB struck a dovish tone in its March policy meeting

This month’s ETF in the spotlight has enjoyed a rush of investor interest as cheap valuations and hopes of a monetary policy pivot make a convincing case for BlackRock’s Europe small cap strategy.

The \$914m iShares STOXX Europe Small 200 UCITS ETF (EXSE) has booked

an impressive \$357m inflows in March, as at 21 March, according to data from ETFbook, as investors look to tap a small cap recovery led by interest rate cuts.

In a research note, DWS noted European small and mid-caps had booked two years of underperformance having “reacted allergically” to central bank rate hikes.

This owes to the fact small caps face higher borrowing burdens than their large cap peers. By the start of March, European

small caps had a net debt to EBITDA ratio of 1.2 versus 0.99 for large cap peers, according to Morgan Stanley.

DWS Global CIO Björn Jesch added: “It can probably be assumed that larger companies refinance themselves to a much greater extent via bonds than small caps, which are more likely to borrow from banks.

“According to the ECB, 80% of corporate loans have a term of less than one year, and so rising interest rates should be reflected in the profit and loss accounts correspondingly quickly.”

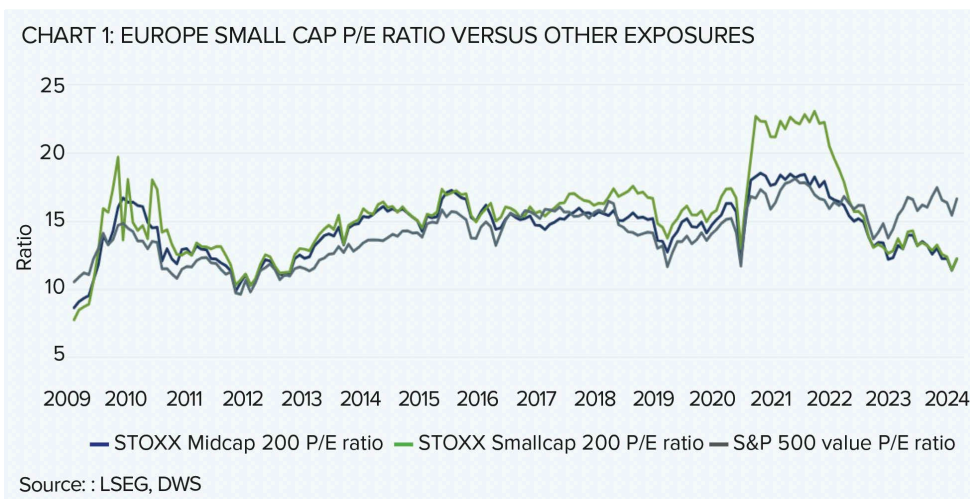
After the March meeting of the European Central Bank (ECB) – where the policymaker held rates steady at 4% and cut growth and inflation forecasts – markets priced in more than 100 basis points (bps) of policy cuts in 2024.

“The ECB significantly reduced the 2024 inflation projection,” Thierry Wizman, global FX and rates strategist at Macquarie, said. “Symbolically important was the 2025 reduction, which implies that the 2% inflation target will be reached by next year.”

Ahead of the tailwind offered by the March ECB meeting, STOXX Europe Small 200 index constituents entered 2024 with higher earnings growth than European large cap equities and prices comfortably shy of all-time-highs, meaning the index’s composite P/E ratio started the year near its lowest level since 2009.

Over the past 25 years to 21 March, European small caps have returned almost 170% versus 25% for the continent’s large caps. Having lagged large cap returns for almost 550 days, the medium-term outlook favours a small cap comeback, said Jesch.

In prime position to capture this potential uptick, BlackRock’s EXSE physically replicates the STOXX Europe Small 200 index comprised of the smallest 200 companies within the STOXX Europe 600 index.



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Location: Borsa Italiana



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Fund Fights

HANetf and HSBC AM enter India tech ETFs

Fund Fights is a series where ETF Stream analyses the strengths and weaknesses of similar ETFs. This month, Europe's first two ETFs capturing India's tech sector go head-to-head

In a further sign of innovation delving into increasingly granular exposures, European ETF investors can now access Indian tech equities via launches from HANetf and HSBC Asset Management.

The first of the two products to debut, the INQQ India Internet & Ecommerce ESG-S UCITS ETF (INQQ), listed on the London Stock Exchange, Deutsche Boerse and Euronext Milan last November.

INQQ tracks the eponymous INQQ index of 26 Indian companies deriving at least 50% of their revenue from sectors including internet services, online retail, broadcasting, media, advertising, travel,

gaming, search engines, payments and social networks.

At the start of March, INQQ was joined by the HSBC S&P India Tech UCITS ETF (HITC), which listed on the same three exchanges. HITC tracks the S&P India Tech index of 38 companies classified as having at least 90% revenue exposure to either the communications, digital tech or software-related subsectors as per FactSet's Revere Business Industry Classification System (RBICs).

In numbers

At first glance, HITC appears to have an edge. Performance leadership has varied

over time, with HITC's and INQQ's underlying returning 33% and 53.4%, respectively, over the past 12 months, as at 26 March, and 6% and -4.3%, respectively, going back to the earliest comparison on 20 March 2022.

However, HSBC AM's strategy has an advantage on the headline cost and early asset gathering fronts.

HITC carries a total expense ratio (TER) of 0.65 versus 0.86% for INQQ. The ETF also amassed \$13m assets under management (AUM), as at 26 March, against \$2m for HANetf's candidate.

Differing approaches

More importantly, investors should acknowledge the two ETFs offer starkly different ways of playing the Indian tech space. On the one hand, INQQ's largest sector allocations are comprised 36.9% of fintech, 15.9% of eCommerce and 10.7% of food delivery companies, providing investors with a more thematic route for targeting the growth of the digitised consumer within India's domestic market.

Conversely, HITC offers a more conventional sector-oriented view of India tech, with a 70.1% allocation to information technology and 23.5% to communications.

Crucially, by offering top allocations to companies such as Infosys – at more than 14% – HSBC AM's candidate provides exposure to Indian companies conducting much of their business globally rather than having a domestic focus.

Interestingly, despite being far more concentrated than the 834-constituent S&P India BMI index, the performance of HITC's underlying has been highly correlated to the broad India benchmark since its calculation began in March 2018.

Alberto Garcia Fuentes, head of asset allocation at ACCI Capital investments, told *ETF Stream*: "It is normal the tech sector displays higher beta.

"If tech companies in India grow, their market cap will increase and the correlation will be even higher."

Investors will have to consider where revenue is being derived from, the degree of correlation they are content with and whether they prefer a more thematic or sector approach when selecting which India ETF best serves their needs.

STAT ATTACK

Ticker	INQQ	HITC
AUM	\$2m	\$13m
12-month return	53.4%	33%
Constituent count	26	38

Data as at 26 March

ETF Buyers Club

The ETF Buyers Club is a community for investors active in the world of ETFs and is the first peer-related group of its kind. Each month, a member of *ETF Stream's* ETF Buyers Club will analyse some of the most important issues facing ETF investors

A new dawn for biotech investments

An exploration of the biotech sector's resurgence, offering a roadmap for savvy investment in a promising yet complex industry

By Bruno Schneller

Amid fluctuating markets and evolving economic landscapes, the biotech sector is emerging from a prolonged period of underperformance, signalling a new era of opportunity for astute investors.

This article provides a comprehensive analysis of the sector's revival, attributing its newfound momentum to a confluence of favourable interest rates, groundbreaking innovations and strategic mergers and acquisitions (M&A).

As we traverse the intricate terrain of biotech investments, we uncover the multi-faceted drivers behind this resurgence, offering an insightful guide to navigating the sector's promising prospects.

The turning tide: Analysing the biotech sector's comeback

For years, the biotech sector struggled to mirror the broader market's gains, with indices like the Nasdaq Biotechnology index

and the S&P Biotechnology Select Industry index experiencing significant downturns. This phase of underperformance, however, is giving way to optimistic recovery signs, thanks in part to a favourable macroeconomic environment and a resurgence in sector-specific innovations.

The correlation between interest rates and biotech investments is unmistakable. Historically low or stabilising interest rates have fostered fertile ground for biotech stocks to flourish, a phenomenon currently unfolding as the Federal Reserve signals a cessation to rate hikes. This macroeconomic pivot, alongside a shifting investor focus towards high-growth alternatives to traditional tech giants, heralds a promising phase for biotech stocks.

Innovation and growth: The biotech sector's lifeline

The year 2023 marked a watershed moment for biotech innovation, with the FDA green-lighting an unprecedented number of new therapies. These advancements are

“The revival of the biotech sector presents a disparate landscape, with the fortunes of companies diverging based on various factors, including the strength of their drug pipelines, financial health and market positioning.”



not mere statistical anomalies but reflect the sector's robust pipeline and its potential to revolutionise treatment paradigms across several disease categories, heralding a new age of medical breakthroughs and, by extension, investment opportunities.

The recent uptick in M&A activities within the biotech sphere underscores the growing confidence in the sector's growth prospects. Notably, the increase in both the volume and value of deals signals a bullish outlook among investors and industry players, further catalysed by regulatory environments becoming more conducive to deal-making.

The investment landscape: Opportunities and pitfalls

The revival of the biotech sector presents a disparate landscape, with the fortunes of companies diverging based on various factors, including the strength of their drug pipelines, financial health and market positioning. This environment underscores the importance of meticulous research and strategic selection, rewarding investors who can identify companies poised for significant breakthroughs or lucrative acquisitions.



In the volatile world of biotech investing, diversification emerges as a critical strategy for mitigating risk. Investors are advised to spread their investments across a spectrum of biotech firms, from established players with solid earnings to high-potential startups at the cutting edge of innovation. Such a diversified approach not only hedges against the inherent risks of the sector but also positions investors to capitalise on its upside potential.

While the pandemic brought unprecedented attention to the biotech sector, its investment appeal extends far into the future, underpinned by demographic trends, the escalating prevalence of chronic diseases, and ongoing innovations in drug discovery and development. These long-term growth drivers suggest that the current resurgence is not merely a fleeting trend but a harbinger of the sector's enduring potential.

Sector analysis: Therapeutic innovations and market dynamics

The biotech sector's promise is vividly illustrated through its rapid advancements in addressing complex diseases. From oncology to neurodegenerative disorders, biotech firms

are at the forefront of developing therapies that not only extend life but also enhance its quality. This therapeutic innovation, coupled with a regulatory environment increasingly supportive of expedited drug approvals, creates a fertile landscape for investments.

The advent of technologies like CRISPR and the rise of personalised medicine are transforming the biotech landscape, opening new frontiers in treatment capabilities and, consequently, investment opportunities. These technologies promise to usher in a new era of precision medicine, where treatments are tailored to the genetic makeup of individuals, potentially revolutionising the management of heretofore intractable conditions.

Embracing the renaissance

As we embark on this journey through the biotech sector's resurgence, it is clear that the landscape is ripe with opportunities for those who navigate it with insight and prudence. The confluence of favourable economic conditions, groundbreaking innovations, and strategic market movements provides a solid foundation for investment in this complex yet promising sector.

The biotech surge is more than just a momentary trend – it represents a fundamental shift towards recognising the sector's potential to drive the next wave of medical breakthroughs and investment gains. For investors ready to delve into this dynamic sector, the promise of contributing to transformative health solutions while achieving substantial financial returns is within reach.

As we look toward the future, the biotech sector stands as a testament to the power of innovation and strategic investment. With careful selection, diversified approaches, and an eye on the evolving landscape, investors can find themselves at the forefront of a sector poised for exponential growth. The biotech surge invites us to explore the intersection of science and investment, offering a unique opportunity to participate in shaping the future of healthcare and reaping the rewards of a sector on the brink of a new era of discovery and prosperity.



Bruno Schneller is managing director of INVICO Asset Management

ETFs to capture building blocks of modern life

‘I would argue at least 5-10% of any global equity budget should be allocated to themes rather than countries’

By Andrew Merricks

A number of years ago I saw a chart that struck a chord with me. It showed how every decade has a theme which, if invested in, produces tremendous returns over a multi-year cycle, but then peaks and enters into a period of wilderness.

For example, the 1970s theme was gold; the 80s was Japan, the 90s was the ‘dot-com’ boom; the 2000s was China and so on. We all know about the FAANGs phenomenon more recently, and currently this appears to have developed into AI – or so my bot tells me.

What has changed most dramatically is the number of apparent themes that are emerging and crucially, the access that we now have to benefit from these themes through the availability of thematic ETFs which can laser focus into specific sectors that would previously have simply fallen under the more woolly tech umbrella.

A four-piece puzzle

The fund I help to run has identified four ‘building blocks’ upon which to develop our thematic approach.

The range of easily accessible exposures available to investors is constantly expanding, though care needs to be taken in trying to identify what is a theme that is truly a multi-year opportunity from those which may turn out to be a passing fad.

It is also important to try to find themes that are actually profitable rather than simply being ideological. Our four blocks are comprised of:

Digital industry – Within this we include AI, cloud computing, cybersecurity, robotics and smart grid.

Healthcare innovation – This currently has biotechnology, genomics and healthcare innovation, the latter including companies that are involved in medical equipment and remote surgery rather than simply being drug related. There are other ideas available in this sector but at the moment healthcare is struggling to gain momentum, but once it does, we will probably expand this area.

New energy and transportation – A similar comment can be made about this ‘block’ as it is proving difficult to match profitability with necessity. There are a plethora of ETFs focussing upon clean energy, individual variants such as solar, hydrogen and nuclear, as well as climate change and decarbonisation offerings, yet these have struggled to deliver a meaningful return since the exuberance that met a Joe Biden win in the last US election. At the moment, we are concentrating more upon the theme of future mobility but know that these other sources are there should we need them.

Online life – In this sector we include internet providers and ecommerce, video gaming and Esports as well as blockchain. Importantly, the ETF world provides access to

FUTURE WEALTH BUILDING BLOCKS (31.01.2024)

Digital Industry	%
CrowdStrike	8.07
X Artificial Intelligence ETF	6.72
First Trust Cloud Computing ETF	6.75
First Trust Cybersecurity ETF	7.70
Amundi Robotics & AI ETF	5.27
ASML HOLDINGS NV	5.18
First Trust Smart Grid ETF	5.00
Total	44.69%

Healthcare Innovation	%
First Trust NYSE Biotech ETF	6.19
Global X Genomics ETF	4.80
iShares Healthcare Innovation ETF	3.96
Exact Sciences Corp	3.01
Total	17.96%

New Energy	%
Xtrackers Future Mobility ETF	4.29
Wisdom Tree Battery	2.93
TESLA INC	2.62
Total	9.85%

Online Life	%
Mercadolibre Inc	5.65
Global X Blockchain	4.79
Vaneck Video Gaming	4.47
KraneShares China Internet ETF	3.83
HAN Emg Markets E commerce ETF	3.73
Global X Video Games & Esports ETF	2.82
Total	25.29%

Cash	2.20%
Total	100%

“The range of easily accessible exposures available to investors is constantly expanding, though care needs to be taken in trying to identify what is a theme”

the emerging market space for the growth in eCommerce and enables investment into China and most recently India, should you want to go down this route.

It is clear that some of these ETFs are not without significant risk and volatility, but

this is why we choose the ETF route rather than individual stocks.

Why ETFs?

You would be forgiven for thinking that any investment outside the ‘magnificent seven’ have been a waste of time, given all of the attention that they have received.

However, one of my favourite themes in which I have been investing for around a decade is threatening to become the next overnight sensation that has been years in the making, much as AI emerged around this time last year. This theme is cybersecurity.

The dominance of the ‘seven’ at the head of the S&P 500 is often the reason that is given for why it is so hard to beat, but the returns of the cyber sector – expressed through the likes of Ark Invest Europe and WisdomTree’s ETFs – tell a different story.

With the US and other elections coming up this year and strange ‘outages’ at Sainsbury, Tesco and Greggs in just the last week as examples, I can only see the demand for cybersecurity increasing substantially.

Interestingly, cybersecurity now features within a couple of defence ETFs that would previously of only held such companies as BAE Systems and Lockheed Martin.

Which leads to why we use ETFs to capture themes. In relatively new sectors such as those mentioned previously, it carries less risk to invest in everything within that sector rather than trying to anticipate which companies will emerge as sector leaders.

Most ETFs are passive and by investing in a passive product you are taking an active decision to invest in everything. ETFs are constructed in very different ways from one-another depending upon the provider – and their process – chosen, but this is a whole different subject that cannot be covered here.

Take the example of the differing performance of two of the leading names in the cybersecurity sector in recent months. CrowdStrike has doubled while Palo Alto Networks has only made 15% over a similar period.

By investing in an ETF, we capture the out-performance of one over the other and with rebalancing that occurs within the structure, we maintain the chance of running winners through their subsequent higher weighting within the given index – subject to the particular process being followed.

If we had tried to stock pick, we run the risk of choosing wrong, even given our exposure

CHART 1: CYBERSECURITY ETF PERFORMANCE

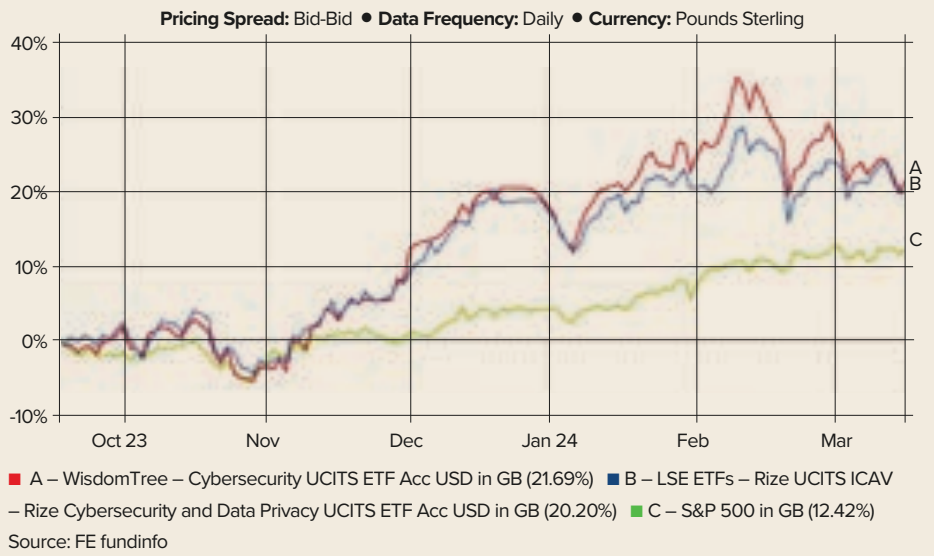
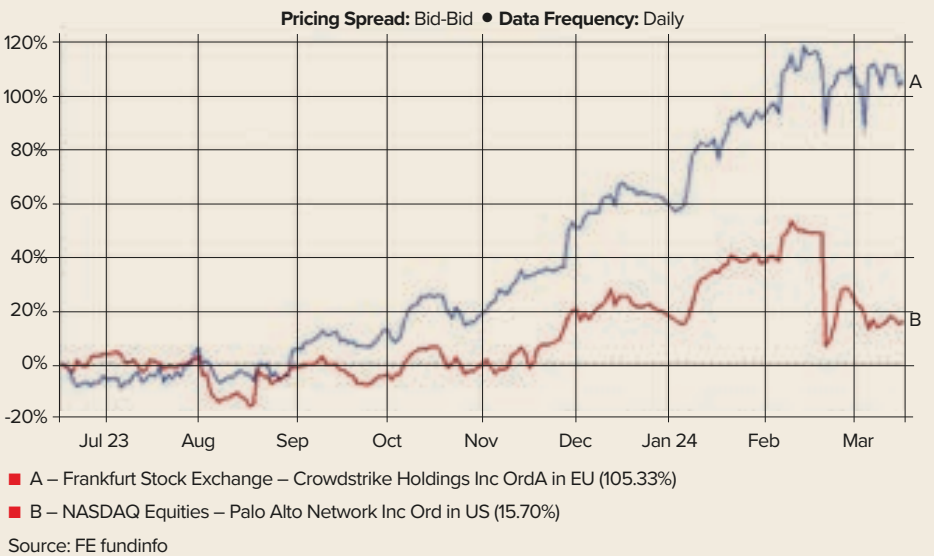


CHART 2: CROWDSTRIKE VS PALO ALTO NETWORK



to the sector. For those of a certain vintage it is akin to Eric Morecambe – of the Morecambe and Wise Show – being aggrieved with Andre Previn for criticising his piano playing, asserting that he was “playing all the right notes, but not particularly in the right order”.

This argument can be made for investing in ETFs covering any theme, particularly relatively new and developing ones.

Should allocation models adjust?

A final consideration that deserves more in-depth scrutiny is the question of whether most current asset allocation models are keeping up with a rapidly changing investment landscape.

Most continue to adhere to the old geographically based frameworks, but I would

seriously question whether at least 5-10% of any global equity budget should not be directed towards themes rather than countries. These themes are truly global and it is striking that many of the ETFs covering them invest across all regions – although the US is still largely dominant.

Investing in themes is not the be all or end all of modern investment, but I would argue that investing in modern times should certainly entail some level of segmented exposure to the themes that increasingly drive so many aspects of modern life.



Andrew Merricks is co-manager of the Margetts IDAD Future Wealth fund

Features & Analysis

The Patient Investor

The wisdom of ignorance

An emerging academic field looks to the past to shed new light on why today's markets are so hard to read

By Justin Reynolds

The markets have once again taken us by surprise, defying last year's gloomy forecasts to hit record highs – for now. The global economy has weathered war, supply shocks, high interest rates, unemployment remaining low and improved corporate earnings confounding expectations that higher borrowing would hit profits. As inflation subsides, confidence is growing that central banks have succeeded – whether by luck or design – in managing a soft landing.

But the figures showing which funds fared best in 2023 are less surprising. Active strategies have continued to struggle, despite uncertain market conditions that in theory work to stockpickers' advantage.

According to data from Morningstar, fewer than a third of actively managed global large-cap equity funds beat the equivalent passive fund in the year to June 2023, and only 3% did so over a 15-year timeframe.

Flagship active funds such as Fundsmith Equity and WS Lindsell Train UK Equity appeared in Bestinvest's *Spot the Dog* report for

the first time, underperforming by 14 and 19% respectively over three years. There are now more assets in US passive funds than active, which account for 40% of worldwide fund assets, up from 14% in 2008. More adventurous passive products seeking to gain an edge over the market have also fared badly, the UBS Investment Returns Yearbook reporting that funds oriented to the momentum, small size, value, high income and low volatility factors all fared worse than their opposite bets.

The asset management industry has never had any illusions about the challenges of reading and beating the market. But it is premised on the belief that it is at least possible. Too much humility is bad for business and cuts against the grain of our rational age that we can interpret complex systems like markets. After all, did not we invent them?

The view from nowhere

An emerging academic field concerned with the limits of knowledge may yield insights into why we cannot help but overestimate our capacity to understand how financial markets work. 'Ignorance studies' might seem an odd subject for an academic world

“The asset management industry has never had any illusions about the challenges of reading and beating the market. But it is premised on the belief that it is at least possible”



customarily concerned with accumulating knowledge. But efforts to understand what we cannot know, as well as what we can, have a rich history, as evidenced by the *Routledge International Handbook of Ignorance Studies*, a weighty volume that runs to 40 chapters ranging across literature, science, law, history, politics and philosophy to define what is beyond knowledge. And Cambridge professor Peter Burke's *Ignorance: A Global History* offers an exhaustive account of how cultures through the millennia have sought to recognise – or deny – what they cannot know.

It may seem rather remote from the hard-headed business of finance, but the study of ignorance can help illuminate why reading the markets seems such a Sisyphean task. Consider, for example, stockpickers' tacit assumption that it is possible to take a birds eye view on the market, to survey it from a privileged perspective from its movements can be anticipated. Scholars of ignorance, however, highlight ages-old insights indicating why that is not just difficult, but logically impossible.

Briefly, if we ourselves are part of a system, we cannot step outside it to look at it from a neutral perspective to take a 'view from nowhere'. Theologians since the Church Fathers have insisted we cannot take a 'gods-



eye' view on creation because we are part of it – as created beings we can never know the mind of the creator. The insight resurfaced in philosophy, famously in the thought of Immanuel Kant, who argued we cannot know the world “as it is in itself”, independently of the particular perspective we have upon it. That we can contemplate the world from a point of view entices us to believe that we can view the world in its entirety. But that is a delusion. Our outlook is always indelibly marked by our particular perspective.

It is essentially the same logic sceptical economists have employed against optimism that we can manage or even interpret complex economic systems. For Friedrich Hayek the current state of a market economy is always and by necessity unknowable because we are part of it, changing how it works by our very presence. More recently, George Soros has argued the market is always “reflexive”. Participants change the path of the market in the very act of seeking to anticipate its direction, in a continual recursive cycle. We can never bootstrap ourselves outside the system of which we are part to obtain an unfettered view from which we might foresee the course of events. Like the horizon it is always ahead and always out of reach.

So understood, the market should be seen

as a volatile, emergent system than as a machine that can be analysed and programmed. Banker turned financial essayist Alex Pollock argues mitigation can simply make uncertainty worse: “All regulators, central banks, and governments are also, along with everybody else, inside the dynamic system that endogenously produces uncertainty. They all take actions of which they cannot know the results, so often enough they themselves create the financial instability they are trying to avoid.” Pollock suggests economists face the same dilemma as historians, who since Herodotus have realised that although human agents create history, its outcomes are not controlled by their actions. Economics is better understood as history than science.

For John Kay and Mervyn King market participants face a world of “radical uncertainty”, which, following an early generation of economists, they define as “the vast range of possibilities that lie in between the world of unlikely events which can nevertheless be described with the aid of probability distributions, and the world of the unimaginable”. But postwar economists, inspired by rapid developments in physics, became increasingly confident that analogous laws could be applied the human worlds of economics, business and finance and attempted

to redefine uncertainty as risk, measurable through models defining a sliding scale of probabilities. “The implication was that risk was something that could be priced. Once it had been priced, risk was tamed. In effect, uncertainty was suppressed by markets.”

Two sides to every question?

Kay and King counsel investors to think in terms of narrative rather than risk. Following the “bounded rationalist” Herbert Simon we must “satisfice”, moving cautiously into the future by venturing reasoned narratives about what may happen, grounded in the information we have to hand. Of course, narratives can be abused too, as they certainly have been in the world of investment. Here, too, ignorance studies has something to say.

‘Agnotology’ – derived from the Greek word for ‘not knowing’ – studies the deliberate cultivation of uncertainty to win favour or sell a product. Practitioners sow doubt by appealing to the common sense supposition that there are always two sides to a question. Consider the tactics used by the tobacco lobby and climate change sceptics – or indeed the alternative narratives constructed by fund managers. There are indeed two sides, but sometimes only if one is patched together by torturing the scant available evidence.

For agnotologists, these are contemporary manifestations of the ancient art of sophistry, as exemplified by the itinerant intellectuals, who, claiming expertise in the craft of argument, taught the youth of classical Athens (in return for a fee) to use reason to reach a desired conclusion. In seeking to expose such instrumentalism Socrates – agnotology’s patron saint – cleared the ground for modern philosophy, developing modes of rigorous argument insisting on the scrupulous definition of the terms of discussion, the careful use of words, and clear, sequential chains of reasoning. Argument should be open-ended, oriented to the truth, rather than designed to prove a premeditated conclusion.

That does not make much commercial sense, perhaps. But they remain useful rules of thumb for investors battered by successive waves of competing narratives. Following students of ignorance, perhaps, we might go back to the past to understand the present so far as it is ever possible to do so.

Justin Reynolds is a freelance journalist and editor of The Patient Investor blog

Implications of AI for cloud computing companies

A key beneficiary of the AI boom

Artificial intelligence: Peak hype?

It is no secret that the potential of artificial intelligence (AI) has been a key driver of equity markets over the past year. The market loves a good story and this is backed by positive earnings momentum and rising stock prices, creating a powerful narrative.

Nevertheless, the extent of AI's influence over market returns might still be surprising. The 'magnificent seven' group of mega-cap technology companies which are perceived as some of AI's key beneficiaries (Apple, Alphabet, Amazon, Meta, Microsoft, Nvidia and Tesla) drove almost 60% of the US equity market's total gains through 2023. This has left the market near its most concentrated in history, with the largest 10% of its stocks making up almost 75% of its capitalisation (as of February 2024). For context, this exceeds the levels seen during the 'dot-com' boom, when hype surrounding the long-term potential of the internet was at its peak. Measured in other terms, the magnificent seven's dominance has left its market capitalisation above that of the entire Chinese stock market, despite the Chinese market being more than twice as profitable.

This situation has not gone unnoticed by companies like Alphabet, which are now cau-

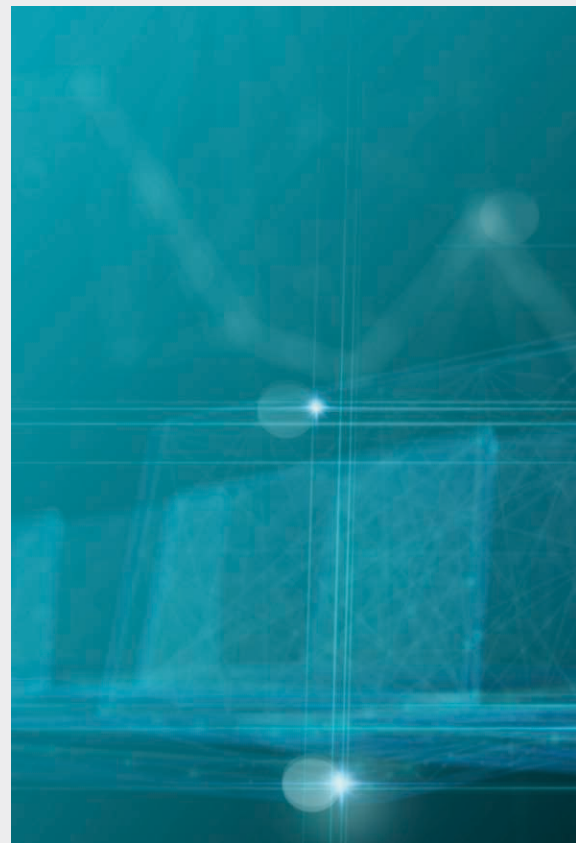
tioning that the market hype surrounding AI may have gone too far in the near term. The economic benefits of new technologies like AI can be extrapolated quickly, but in practice may take many years to reflect in corporate profitability. This could easily be the case with AI, particularly given the social, political and regulatory scrutiny currently being placed on technology companies around the world.

As with any new technology, it is not clear how things will play out long-term. We see some comparisons between the current market backdrop and that of the Dotcom era; many hot AI stocks might follow key Dotcom names like Amazon to become very successful companies, but not all of today's big AI names will be the winners of tomorrow – some will fail. Rather than following the hype, it is therefore better to determine areas where AI will be able to deliver real improvements in the near term, even if they might not be obvious (and ideally where they are not priced into markets).

Cloud computing: A key AI beneficiary

Despite the investor hype surrounding AI manifesting largely within the magnificent seven companies' high valuations, as the

“We see some comparisons between the current market backdrop and that of the Dotcom era; many hot AI stocks might follow key Dotcom names like Amazon to become very successful companies, but not all of today's big AI names will be the winners of tomorrow – some will fail.”



technology continues to advance its integration will become a game-changer for a broader array of companies across many industries. At the forefront will be cloud computing, where many businesses are able to leverage its benefits using their existing expertise and access to vast technological resources. Indeed, some cloud companies are already leveraging AI to improve decision making and acquire further competitive advantages over their less-innovative incumbent competitors.

For example, AI can allow cloud service providers to develop automatic processes that analyse large volumes of data to predict demand and allocate resources accordingly. This can reduce the need for manual intervention in areas like server monitoring, maximising performance and minimising downtime. In turn, this can allow them to scale their infrastructure dynamically to meet the fluctuating demands of their customers, which can improve their operational efficiency and reduce their costs.

It is well known that companies are already using AI chatbots to enhance customer support via instant 24-hour assistance while also reducing staffing costs.



However, this is just the tip of the iceberg. They are also leveraging cutting-edge AI technologies in such as machine learning to develop intelligent solutions that adapt to user behaviour and provide more personalised experiences.

Cybersecurity is another AI hotspot where threats are become increasingly sophisticated; it can be used to help detect and prevent potential attacks in ways which humans may overlook. The technology has numerous applications and, as a result, it provides another important tailwind for the ubiquitous adoption of cloud computing technologies across all sectors of the economy.

Fidelity Cloud Computing UCITS ETF

The Fidelity Cloud Computing UCITS ETF provides investors with a transparent, cost-effective means of gaining diversified passive exposure to the cloud computing theme (characterised by the delivery of computing services over the internet, including cloud infrastructure, platforms and software providers).

Its investment objective is to provide a net total return which reflects that of the Fidelity

Cloud Computing ESG Tilted index, which is itself formed through the identification of companies with high-purity exposure to the theme via analysis of revenue data and the use of natural language processing to analyse large amounts of public and proprietary natural language data. It also ap-

plies quality and ESG screens to help avoid stocks which may represent high levels of idiosyncratic risk, with the goal of providing the exposures our clients require.

Discover our range of innovative ETFs powered by Fidelity research

Important information

This information is for investment professionals only and should not be relied upon by private investors. The value of investments can go down as well as up so you may get back less than you invest. Investors should note that the views expressed may no longer be current and may have already been acted upon. Reference to specific securities should not be interpreted as a recommendation to buy or sell these securities and is only included for illustration purposes.

This fund invests in overseas markets and so the value of investments can be affected by changes in currency exchange rates. This fund uses financial derivative instruments for investment purposes, which may expose the fund to a higher degree of risk and can cause investments to experience larger than average price fluctuations. This fund has, or is likely to have, high volatility owing to its portfolio composition or the portfolio management techniques. The ETF tracks an equity index and as a result the value of the fund may go down as well as up. Performance data is based on the net asset value (NAV) of the ETF which may not be the same as the market price of the ETF. Individual shareholders may realise returns that are different to the NAV performance.

Investments should be made on the basis of the current prospectus, which is available along with the Key Investor Information Document, current annual and semi-annual reports free of charge on request by calling 0800 368 1732. Issued by FIL Pensions Management, authorised and regulated by the Financial Conduct Authority. Fidelity International, the Fidelity International logo and F symbol are trademarks of FIL Limited. UKM0324/386483/SSO/NA



How do thematic ETF issuers balance purity, diversification and liquidity?

Tensions between the three are mitigated through theme-specific approaches

By Lauren Gibbons

Theme purity versus diversification and liquidity can often be a difficult balance to strike for ETF issuers when dealing with nascent megatrends. The question of how issuers address this challenge is increasingly rele-

vant as thematic ETFs continue to establish themselves as a portfolio construction tool to add risk and potentially generate alpha.

In addition, the anticipation of central bank rate cuts across the globe – set to benefit growth-orientated companies – also underscores thematic ETFs’ increasing relevance as the year progresses.

Theme purity might seem like the obvious priority when issuers work with the index provider to construct a thematic ETF, however, liquidity issues can quickly arise from an overconcentration of small, illiquid stocks. Conversely, larger stocks that provide liquidity might not offer the purest exposure to a theme.

Meanwhile, diversification also remains central as investors allocate to thematic ETFs to add variation to their core global equity allocations. To shed light on how issuers navigate these complexities, *ETF Stream* spoke with four ETF issuers – BlackRock, Invesco, WisdomTree and Legal & General Investment Management (LGIM) – about their strategies for tackling these competing priorities.

Weighting to mitigate liquidity issues

When balancing liquidity against thematic purity, Christopher Mellor, head of EMEA equity ETF product management at Invesco, said a critical factor is how an ETF is weighted. “Weighting has a big impact on how much

exposure you get to the theme, but it also has a big impact on the potential liquidity of the underlying stocks within the basket or portfolio,” Mellor told *ETF Stream*.

The liquidity of the basket of stocks is what drives the decision to apply an exposure weighting, an equal weighting or a market-cap weighting, Mellor explained. If there are a sufficient number of liquid stocks, Invesco will opt for either exposure weighting or equal weighting. LGIM hurdles their high exposures to small and mid-cap stocks through a modified equal weighting approach.

Aanand Venkatramanan, head of ETFs for EMEA at LGIM said: “Our indices...know how much assets under management (AUM) we track, and based on the AUM, the weight of some of the small-cap names, or the lesser liquid names, are capped.”

Similarly, Omar Moufti, thematic and sector product specialist at BlackRock, said all strategies will take into account the liquidity and related market cap of the underlying stock.

In addition, when a theme has greater monopolistic characteristics, such as one that has significant exposure to utilities, like water or clean energy, then BlackRock will have a higher focus on the market cap weighting.

“Where we think there are not really that many barriers to entry, and we consider that the high-level theme will be the main driver of growth across companies, then we lean more towards an equal weighting approach,” Moufti added.

Pierre Debru head of quantitative research and multi-asset solutions at WisdomTree, said: “You have to be very careful about the liquidity...of the portfolio. It is about not creating a huge concentration in very small, illiquid stocks.”

Debru added megatrends at an early stage need to be equally weighted as the companies are still developing and winners could potentially come from anywhere. For a more developed theme, he said it “may already have a value chain in place and then maybe the weighting that takes into account the part of the value chain is going to be more relevant”.

“The weighting needs to be adapted to the theme and that is why expertise is key in the designing phase.”

Selecting stocks aligned with the theme

Determining the alignment of a stock with a specific theme is another challenge that

“When balancing liquidity against thematic purity. Weighting has a big impact on how much exposure you get to the theme, but it also has a big impact on the potential liquidity of the underlying stocks within the basket or portfolio.”

should arguably be addressed before attempting to balance liquidity, theme purity and diversification.

This is important to consider, as companies with lower thematic purity levels are more likely to engage in activities – and more specifically derive revenues – from sources that are not central to the theme.

On the flip side, it is hard for an ETF to achieve absolute, undiluted exposure to a specific theme, as companies often operate across multiple business lines, leading to a natural dilution of the strategy’s thematic concentration.

To this point, Mellor said using revenues to derive theme purity may become complicated, particularly for larger stocks.

“Much like tech, in the realm of robotics, the leading manufacturers are typically part of larger industrial conglomerates, and so creating a thematic ETF that aims for significant exposure can be challenging if the theme only represents a small fraction of the company’s revenues.

“I would be very cautious of a thematic product that just holds the usual suspects because it is not really exposed to a particular theme – it is exposed to many themes.”

Theme-related revenues might also complicate judging how well aligned a stock is with a theme, as they are backward-looking and do not necessarily reflect how the company will operate in the future.

When LGIM identifies which stocks are related to a theme, Venkatramanan said: “As an example, we then pick the most dominant wind turbine manufacturers of tomorrow, if there is a new company that’s coming up with a very strong pipeline, we have visibility into that rather than just looking...at the financials and then picking a stock.”

However, drilling down too much on a theme can mean that some players are left out and might stand to become the ‘winner’ of the forward-looking theme in 15 years.

For this reason, “stock selection is very much about the balance between diversification and purity”, Debru told *ETF Stream*.

For instance, adopting a diversified strategy can enhance investors’ chances of investing in the next ‘big success’ while simultaneously reducing the risk of overlooking such an opportunity.

“Yes, we want purity. Yes, we want to invest only in companies that are very relevant to the space but it does not mean that we have to be overly selective either.”

Final word

Philosophies toward constructing a thematic ETF depend heavily on how the issuer prioritises each of the three elements. To some ETF issuers, theme purity might remain central to construction, employing only an exposure weighting approach to all themes to maximise purity.

However, each of the aforementioned issuers adopts a more conservative view, seeing more value in balancing each metric to achieve the best outcome for investors.

“Liquidity matters as much as thematic exposure,” Mellor explained.

Aside from prioritising striking a balance between all three elements, above all, if it does not look feasible to launch a thematic ETF at the initial stages, then the issuer may simply not launch the ETF.

Mellor added, “Ultimately, it depends on the analysis that [Invesco] runs when looking to launch an ETF. Is the basket going to be tradable? How does it work? How well does it work in the real world?”

“There are some themes that we have looked at where the theme makes sense, but getting meaningful exposure through a publicly listed equity route may not be the appropriate way of doing it.”

Lauren Gibbons is a reporter at *ETF Stream*



STOXX's Singhal: Thematics could follow sectors in becoming a portfolio staple

There is nothing passive about indexing and nowhere is this more true than in the dynamic landscape of future themes

A key evolution to watch within thematic strategies is not just their increasing sophistication but their growing presence within mainstream investment portfolios, according to Arun Singhal, managing director and global head of product management at STOXX. Index construction in equities has shifted through rapid tides over the past

century. From popular market cap-weighted benchmarks to small caps and sectors decades ago, to smart beta and now a growing range of increasingly granular future themes.

Facilitating this latter shift has been the proliferation of new data sets – from specific revenue segments, to wording in company documents, to patent filings – alongside the technology necessary to synthesise vast

amounts of raw inputs and wrap them within transparent strategies.

What are the key differences between today's rules-based thematic strategies and those a decade ago?

A decade ago, thematic investing – and investing broadly – was in a very different shape to where it is today. It is the age-old buzz words, technology, data, the acceleration of this entire industry has allowed us to capture more nuanced exposures and markets. A decade ago, you were looking at regional or revenue-based allocation of firms. Today we are still using revenue to capture different themes, but a lot of other data sets and signals are now available. Another key difference is the volume of thematic strategies.

Historically, the differences are that technology and data have continued to allow us to push the envelope in capturing narrow-based exposures for different themes in a systematic, rules-based and transparent manner. Transparency is provided through technology and data and the ability to look through within the selection process of securities.

What are some of the key efficiencies shortening the time-to-market on new thematic strategies?

When you look at the curation of data, we need to extract information at the constituent level. Companies have a wealth of data about their businesses and, decades ago, it was about market capitalisation or earnings. Now, you can extract revenues of a company geographically. A decade ago, people would be doing that manually by analysing financial reporting. Now, technology has allowed us to scrub those financial reports aggregated across the majority of companies.

Companies are not mandated to disclose their revenues from a geographical location or sub-product level, but you can find that information in the sub-footnotes in the financial statements these companies put out.

How have sources of data evolved to adapt to more granular and esoteric exposures?

There is no shortage of data that hits our radar, it is having the ability to know how that data can be translated in a transparent



manner in an index construct. That leads us to things like patents, revenues, geographic location. Just within sustainability, there are large amounts of data. We just launched a biodiversity index and the amount of natural capital and biodiversity data out there is vast, but the ability to synthesise it and understand how to curate it into a rules-based process is the biggest challenge for index providers.

How will the role of NLP and AI develop within indexing?

Natural language processing (NLP) allows us to dig into data sets which are not synthesised. Companies put out a lot of information, much of which is done informally rather than formally.

NLP specifically, within the AI umbrella, allows us to process vast amounts of data, from board reporting and earnings to CEO comments. The challenge is staying true to who we are as index provider: transparency, consistency, breadth and depth. Right now the challenge is not to blindly take that data and run, but ask, is it being captured in a consistent manner, does it have the breadth and depth and replicability to put it into an index?

The industry is moving at a rapid pace where there is a desire to capture themes much more quickly before they have any

sort of maturity at all. And that's where we are trying to push the boundaries beyond revenues to see what other data sets we can use. Where you see unstructured data, that is where NLP and AI come in. For some themes such as the Metaverse, which are earlier on in the maturity curve, you need more creativity.

How has demand for thematic strategies evolved?

People have always been after exposures or signals or information that will give them alpha. What has changed is that the broader consumer has been allowed to access this information. A decade ago, folks were going in and doing these processes manually. Now what technology and thematic investing have done is to expand the access. It is democratizing investing. Just like you can now get a purchase delivered to your doorstep in 24 hours with the lowest price, any consumer can get the same intelligence and insight on a company packaged in a transparent manner in a thematic index.

How have the challenges of thematic index construction changed?

One of the biggest things we have done at STOXX over the past two years is reinforced our teams that evaluate our index method-

ologies. This is one of the challenges index providers have – they come from a world of broad-based passive investing. There is nothing passive about indexes. We have to continually monitor and evaluate index methodologies and enhance them. This is the challenge in our industry and so at STOXX we do not follow a 'set it and forget it' approach.

A significant portion of our roadmap and resources for this year is dedicated to enhancing index methodologies, having consultations, meeting with the marketplace, understanding if the methodology is still meeting the market needs and to anticipate anything we need going forward.

How do you expect the process of thematic index construction to change over the coming years?

What is going to evolve is the embracing of thematic investing within the mainstream investment portfolio. If we look at the sheer size and adoption of sectors, who is to say sectors could not have been called themes fifty years ago when they were created?

I think thematic investing is going to be more and more embraced within a broad-based investment allocation within portfolios and it is time to start evaluating it along the lens of sectors.

ARK Invest Europe faces challenge to win over fund selectors

Cathie Wood's stardust will certainly garner plenty of attention across Europe, but translating that into fund selector asset growth might require a change of approach

By Theo Andrew

Cathie Wood's ARK Invest Europe will face a significant challenge to win over Europe's professional investor base and shake off the FOMO-stock retail label born out of its US endeavours.

Fund selectors are sceptical about where the group's asset growth will come from in Europe and whether Wood's "evangelical gut feel" investment approach will resonate in a market dominated by advisors and institutions.

ARK acquired thematic specialist Rize ETF from Martin Gilbert's AssetCo last September in a cut-price deal of £5.25m. Since then, Wood has been using her star power on the continent, conducting a European roadshow in a bid to win over fund selectors, many of whom remain unconvinced.

Fund selector snub

Terry McGivern, senior research analyst at AJ Bell, said Rize ETF will benefit from media-savvy Wood, who has proven she can woo the retail market in the US, but questions whether her "shoot from the hip style" can be replicated in Europe.

"I do wonder which part of the market asset growth will come from," he continued. "I suspect it will be in the more narrative, media-led FOMO end which is often dominated by retail investors, rather than institutional or adviser-led money."

"There is a lot of fixation on US managers coming to Europe to launch active ETFs, but what are they doing that is different? It is a big existential crisis that is coming"

"Her often clunky timing of entry and exits of large positions has allowed them to see big gains at times, but of late has also seen them suffer large and sustained drops. That sort of volatility does not lend itself well to being picked up and included in portfolios run by professional fund selectors."

The group will also have to overcome the idea that ARK Investment Management is a wealth destroyer. According to Morningstar research, the group wiped out a total of \$14.3bn of shareholder value over the past 10 years - the most of any fund house.

Andrew Limberis, investment director at Omba Advisory & Investments, said he was "sceptical" on the impact ARK would have in Europe, even in a market where an active approach to thematic could benefit European investors.

"All being said, even with potential benefits and sound reasoning of an active thematic approach, it is going to be a very difficult job to convince European investors," he added.

Active thematic opportunity

In the months prior to the sale, AssetCo wrote down the value of Rize ETF by roughly £5m,



citing the Ukraine war and "subsequent market jitters" as a reason for damaging its thematic focus.

At the time of acquisition, Rize ETF had roughly \$452m assets under management across 11 ETFs, with its investor base primarily made up of professional investors, something the group hopes will give ARK Invest Europe the platform to succeed.

Rahul Bhushan, head of index at ARK Invest Europe, said: "Rize ETF's investor base has always been wholesale clients - Europe is highly intermediated. There might be retail at the end of the chain, but we will be focusing on wholesale to build the business."





He added there is a growing demand for multi-thematic ETFs – such as the flagship ARK Innovation ETF (ARKK) – from fund selectors who cannot be bullish around a single theme such as AI or cybersecurity.

ARK Invest Europe is set to launch its first three ETFs in Europe in the coming month, including ARKK, as it looks to take advantage of the burgeoning active ETF space in Europe.

“The ETFs will be a great addition to the active thematic product suites in Europe, there is nothing like this which is backed by such rigorous research,” Bhushan said. “The launches will be an interesting test case to see how the market opens up. We

believe markets will open up, that is the feedback we have been getting.”

He added the group’s strong identity will help them come out on top of growing competition in the active ETF space, especially with US asset manager’s increasingly eyeing Europe as the next big growth market.

“There is a lot of fixation on US managers coming to Europe to launch active ETFs, but what are they doing that is different? It is a big existential crisis that is coming,” Bhushan warned.

“Many of these managers will struggle because they do not have an identity and the market will hollow out over the next decade.”

Can investors be won round?

While it may take time for the group to shake off its retail focus, there are some investors who share Bhushan’s bullish sentiment.

James Penny, UK CIO at Tam Asset Management, said market volatility has not helped ARK over the previous couple of years but welcomed their addition to the European market. “ARK is innovative with plenty to bring to the market to help boost both alpha and diversification for industry and retail portfolios,” he said. “In that respect, its entry into the European market is certainly one to be celebrated by both retail and professional investors.”

Karin Weiderkehr, co-founder of discretionary asset manager IMP AG, agreed, noting the addition of an active thematic investor was “great” for professional investors.

“ARK’s entry into Europe is a very positive development and we are a big fan of Cathie,” she said. “It is great to see thematic develop from a broad index approach into something more active.”

However, Wood remains a divisive figure in investing and some believe she may have to take more of a backseat to succeed. “It may require the business to step out of Cathie’s shadow and reign in their approach for them to penetrate the institutional market,” McGivern said. “But I do not see that anytime soon, given she is synonymous with the brand and it is hard to separate where Cathie ends and ARK starts, in its current form.”

ARK Invest Europe will have to work hard to win investors but there are signs there is appetite for their high conviction approach in Europe. Challenges around distribution will also have to be overcome, with Bhushan noting the group has been working hard to build out its distribution capabilities – an area typically outsourced in the US, but not in Europe.

In addition, Wood has previously made clear Europe is a stepping stone to a global market for ARK – with the group eyeing growth in Asia and Latin America via the highly valuable UCITS structure.

For now, some fund selectors remain unsure. “I am not, in all honesty, expecting to see their funds proliferate widely into multi-asset fund ranges and MPS in the near future,” McGivern predicted.

Theo Andrew is news editor at ETF Stream

Targeting decarbonisation outcomes

Preparing portfolios for a low-carbon world using ETFs

With the climate challenge becoming ever more urgent, investors are increasingly looking to include climate investing solutions into their portfolios. The decarbonisation of portfolios is one of the most important objectives for climate investing. Climate Transition Benchmark (CTB) ETFs or Paris Aligned Benchmark (PAB) ETFs can be an efficient way to achieve portfolio decarbonisation targets.

The JPM Carbon Transition Global Equity (CTB) UCITS ETF (JPCT) has been developed in line with the Paris Agreement and is designed to help investors manage the risks of climate change, capture the opportunities and contribute to solutions.

A framework for investing in the carbon transition

JPCT uses a proprietary research framework that aims to determine how well companies are prepared for the carbon transition by evaluating companies across three key pillars:

- **Managing emissions:** Looking at companies' production of direct (Scope 1) site emissions

and indirect (Scope 3) consumer emissions and opportunities, as well as how they plan to manage and reduce emissions.

- **Resource management:** How companies manage resources, including electricity (indirect "Scope 2" emissions from electricity usage), water and waste.

- **Managing climate-related risks:** Both physical e.g. how well a company is positioned to withstand physical risks as a result of climate change; and reputational e.g. how well it incorporates sustainability considerations into its business.

Analysis of company performance against these three pillars forms the basis of our carbon transition investment framework. The aim is to provide a comprehensive view of the carbon transition across global sectors and regions that takes into account upside as well as downside risks.

Using alternative data to broaden the opportunity set

Traditional sources of corporate information, such as company reports and analysis from third-party data providers, are useful in



KEY PILLARS FOR CARBON TRANSITION EVALUATION

Managing Emissions	Managing Resources	Managing climate-related risks
<p>Site emissions Reduce direct emissions and shift towards greener forms of energy</p> <p>Consumer emissions & opportunities Benefit from a shift in consumer demands towards low carbon alternatives</p>	<p>Electricity management Reduce indirect GHG emission from the usage of electricity</p> <p>Water management Improve the sustainability of water flow management</p> <p>Waste management Reduce waste materials, both hazardous and non-hazardous</p>	<p>Physical risk Physical risks from extreme weather conditions</p> <p>Reputational risks Improve climate stewardship</p>

analysing whether companies are managing their businesses sustainably. However, this data can be inconsistent.

To address this issue, we rely on our expertise in artificial intelligence and big data, and a proprietary machine learning tool, ThemeBot.

This tool uses natural language processing to screen more than 10,000 stocks globally, and rapidly analyses hundreds of millions of data sources – such as news articles, company reports, earnings transcripts, and broker



“ThemeBot uses natural language processing to screen more than 10,000 stocks globally, and rapidly analyses hundreds of millions of data sources to identify stocks with the highest exposure to a theme”

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research – to identify stocks with the highest exposure to a theme.

JPM Carbon Transition Global Equity (CTB) UCITS ETF*

Our research framework is used to construct the J.P. Morgan Asset Management Carbon Transition Global Equity index, a proprietary benchmark that is designed to align with the European Union’s Climate Transition Benchmark standards. The index leans into companies that are best prepared, and away

from companies that are most exposed, to carbon transition.

By closely tracking our carbon transition index, JPCT* aims to provide a core global equity exposure, without taking regional and sector bets, and maintains a low tracking error to the MSCI World. Our approach ensures at least a 30% reduction in carbon intensity relative to the MSCI World and a 7% year-on-year rate of decarbonisation. JPCT* launched in November 2020 and has assets under management of over \$1.2bn.



The case against a crypto allocation

No utility other than speculation

By **Nicolas Rabener**

Another boom in cryptocurrencies could kick off in 2024 as the SEC finally approved multiple bitcoin ETF applications that have been years in the making. The Grayscale Bitcoin Trust (GBTC) still dominates with \$26bn assets under management (AUM), but iShares' Bitcoin Trust (IBIT) quickly accumulated \$10bn.

Fidelity's Wise Origin Bitcoin fund ranks third with more than \$6bn AUM, but this can be considered disappointing given that Fidelity manages more than \$5trn, and has an outspoken cryptocurrency enthusiast, namely Abigail Johnson, as a CEO. Buying coins or tokens via digital wallets has been painful or prohibitive for most investors, so being able to buy at least bitcoin like any stock on the exchange is a game changer. However, easier access to an investment

product does not make it a sound investment proposition per se.

In this article, we will evaluate the case for a cryptocurrency allocation.

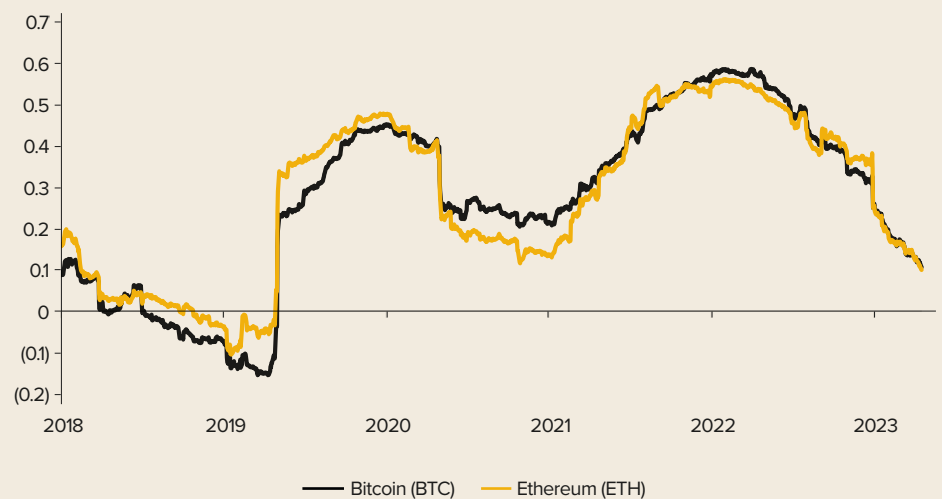
Crypto as diversifier

Investors' universe of investable assets steadily expands as asset managers in public and private markets continue to launch new products, which has made investing more complicated. However, we can reduce this complexity drastically by eliminating any products that are highly correlated to equities or fixed income, which are the cornerstones of most investors' portfolios.

Intuitively, cryptocurrencies should not be correlated to stocks or bonds, but were actually during certain periods. Measuring the 12-month rolling correlation of the two largest cryptocurrencies by market capitalisation, namely bitcoin (BTC) and ethereum



CHART 1: CORRELATIONS OF BITCOIN & ETHEREUM TO NASDAQ INDEX



Source: Finominal

CHART 2: CORRELATIONS OF TOP 10 CRYPTOCURRENCIES (2020-2024)

	BTC	ETH	BNB	SOL	XRP	ADA	AVAX	DOGE	TRX	LINK
BTC	1.00	0.80	0.62	0.53	0.52	0.64	0.55	0.33	0.60	0.67
ETH	0.80	1.00	0.64	0.61	0.56	0.68	0.58	0.29	0.62	0.76
BNB	0.62	0.64	1.00	0.53	0.48	0.56	0.54	0.20	0.55	0.59
SOL	0.53	0.61	0.53	1.00	0.44	0.54	0.56	0.20	0.45	0.56
XRP	0.52	0.56	0.48	0.44	1.00	0.55	0.46	0.21	0.56	0.56
ADA	0.64	0.68	0.56	0.54	0.55	1.00	0.64	0.28	0.57	0.68
AVAX	0.53	0.58	0.54	0.56	0.46	0.64	1.00	0.23	0.46	0.57
DOGE	0.33	0.29	0.20	0.20	0.21	0.28	0.23	1.00	0.26	0.29
TRX	0.60	0.62	0.55	0.45	0.56	0.57	0.46	0.26	1.00	0.60
LINK	0.67	0.76	0.59	0.56	0.56	0.68	0.57	0.29	0.60	1.00

Source Finominal

(ETH), to the Nasdaq index shows highly positive correlations in 2020 and 2022.

Although the average correlation of both coins to the Nasdaq was only 0.3 since 2018, the high correlations are concerning as most investors have exposure to technology stocks via their equity allocation. Over the last nine years, the upside beta of BTC to the stock market was 0.71 and the downside beta was 1.43, which is an unfavourable ratio, and considerably worse than that of gold, which features an upside beta of 0.09 and downside beta of 0.03. Stated differently, BTC and ETH do not offer uncorrelated returns and offer less diversification benefits than likely expected (Chart 1).

Correlations of top 10 crypto

The correlation of BTC and ETH to the Nasdaq index also highlighted identical trends, which means that BTC and ETH are highly

“Being able to buy at least bitcoin like any stock on the exchange is a game changer. However, easier access to an investment product does not make it a sound investment proposition per se.”

correlated to each other. We demonstrate this by calculating the correlations of the top 10 cryptocurrencies by market capitalisation in the period between 2020 and 2024.

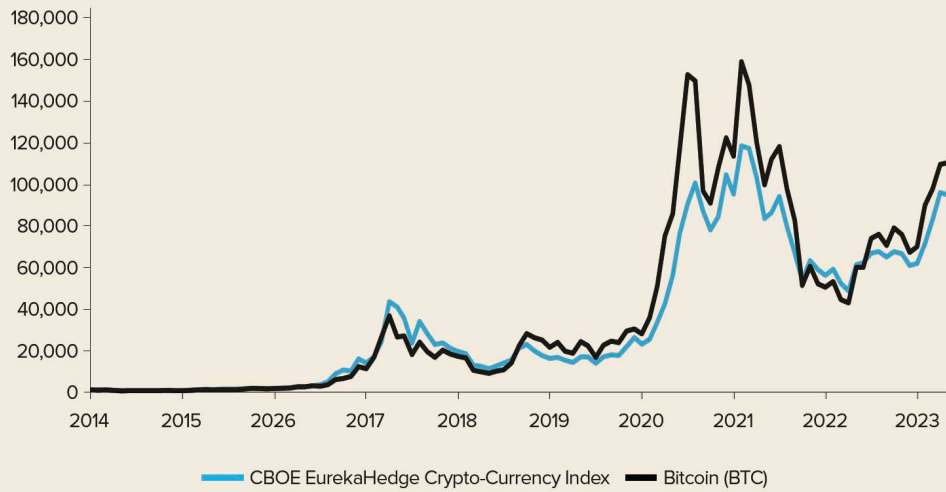
We observe that the correlations were all positive and ranged from 0.2 to 0.8, which is surprising as they seem to have different use cases, i.e. bitcoin is considered digital gold, ethereum is used to power most decentralised

apps, ripple (XRP) focuses on payments, and some, like dogecoin (DOGE), have no obvious use case at all. Naturally, this implies that these 10 cryptocurrencies are driven by systematic rather than idiosyncratic factors (Chart 2).

Active management in crypto

An investor seeking to invest in cryptocurrencies has the choice of thousands of coins

CHART 3: CRYPTOCURRENCY HEDGE FUNDS VERSUS BITCOIN



Source: Eurekahedge, Finominal

TOP 50 APPS IN IPHONE STORE (MARCH 24)

Rank	App	Category	Rank	App	Category
1	Temu	Shopping	26	Wood Nuts & Bolts	Games
2	Threads	Social Networking	27	McDonald's	Food & Drink
3	Tik Tok	Entertainment	28	Robbox	Games
4	Google	Utilities	29	Life360:	Social Networking
5	SHEIN	Shopping	30	Walmart	Shopping
6	YouTube	Photo & Video	31	Uber	Travel
7	Instagram	Photo & Video	32	Township	Games
8	CapCut	Photo & Video	33	Pinterest	Lifestyle
9	ChatGPT	Productivity	34	Roku	Entertainment
10	Google Maps	Navigation	35	Messenger	Social Networking
11	Gmail	Productivity	36	Airbnb	Travel
12	Facebook	Social Networking	37	Discord	Social Networking
13	WhatsApp	Social Networking	38	Reddit	News
14	DoorDash	Food & Drink	39	Google Chrome	Utilities
15	MONOPOLY GO!	Games	40	Duolingo	Education
16	Microsoft Copilot	Productivity	41	Apple Sports	Sports
17	Cash App	Finance	42	Ticketmaster	Entertainment
18	Vocal Range Finder	Music	43	XX Corp	News
19	Block Blast	Games	44	Amazon Prime Video	Entertainment
20	Max	Entertainment	45	Uber Eats	Food & Drink
21	Snapchat	Photo & Video	46	Domino's Pizza USA	Food & Drink
22	Netflix	Entertainment	47	Peacock TV	Entertainment
23	Amazon Shopping	Shopping	48	PayPal	Finance
24	Spotify	Music	49	Nike	Shopping
25	Telegram	Social Networking	50	Hexa Sort	Games



and tokens, which may be overwhelming, especially when considering that most are not easily accessible via ETFs or futures, and require setting up complicated digital wallets. However, the large and complex universe should make cryptocurrencies a perfect playing ground for active managers.

We plot the performance of the CBOE EurekaHedge Crypto-Currency index, which represents an index of hedge fund managers that can take long and short positions in the entire universe of cryptocurrencies. Given the typical performance fees of hedge funds, these are highly incentivised fund managers who should be laser-focused on producing attractive and uncorrelated returns.

However, we see that these hedge fund managers do not seem to provide anything but exposure to BTC, including drawdowns of more than 80%. Intuitively, these active managers should have provided consist-



“The use case for cryptocurrencies is less clear, despite the massive amount of talent that entered the space and billions of dollars that were invested into projects over the last few years.”

ently positive returns by trading against the hordes of unsophisticated retail investors that dominate the cryptocurrency space (Chart 3).

Use case of crypto

Investing in stocks and bonds means providing capital to companies and governments for productive purposes, while investing in currencies and commodities is more about speculation. However, there are naturally clear use cases for the securities of the lat-

ter two asset classes, e.g. oil is utilised in industrial and consumer products and the Swiss Franc represents the currency of the country Switzerland.

The use case for cryptocurrencies is less clear, despite the massive amount of talent that entered the space and billions of dollars that were invested into projects over the last few years.

We can simply look at the top 50 apps on the iPhone store and it is challenging to identify any apps that are built on block-

chain technology or use cryptocurrencies as primary means for payments (Chart 4).

Further thoughts

Investing has become more complex and despite more regulations, not less risky. Simplifying portfolios is crucial for achieving success, as it offers investors clarity and sharper focus.

Allocating to cryptocurrencies increases the complexity as coins and tokens are complicated. However, the case for or against an allocation to cryptocurrencies can be put into a simple question: should you invest in something that is often correlated to equities, where active managers struggle to generate attractive returns, and that has little utility aside from speculation?

Nicolas Rabener is founder and CEO of Finominal

Nvidia's rapid domination of theme and sector ETFs

NVDA concentration 'a meaningful consideration' for investors

By Jamie Gordon

Nvidia's vast size and toe-curling rally may now be the daily chit-chat of trading desks and taxi drivers alike, however, in ETF land the question is how the chipmaker has come to drive a third of the returns in some thematic and sector ETFs after quadrupling its footprint in little over a year.

After AI mania and global processing unit (GPU) demand from data centres drove 239% Nvidia price gains last year, Q4 earnings released in February – including an almost \$2bn revenue beat – fanned the already healthy flame of investor interest. Shares surged a further 88% in Q1, taking Nvidia to a colossal \$2.3trn market cap.

Future theme driver

Naturally, these gains are reflected within passive ETFs holding the stock to the extent that their underlying benchmarks allow.

Among these are thematic ETFs capturing semiconductor and AI megatrends, with the Amundi MSCI ACWI Semiconductors ESG Screened UCITS ETF (CHIP) being the posterchild of the Nvidia effect.

CHIP has established itself as the best-performing non-blockchain UCITS ETF over the medium term, skyrocketing 143.1% between the start of 2023 and 22 March this year.

Nvidia's role in this has been anything from tangential. While its weight in CHIP's underlying index more doubled from 14.2% to 33.5%, data from Bloomberg and Amundi revealed a considerable 74.4% of the ETF's gain through the period can be attributed to the chipmaker.

Although ETFs are often chosen as tools to gain diverse exposures to future themes – and Nvidia's current weighting tests the limits of the 20/35 rule applied to CHIP's underlying – it is not the only thematic ETF enabling large single stock bets on Nvidia. In fact, others, such as the Global X Robotics

“Investing in thematic funds is like placing a trifecta bet at the horse track. You are trying to get three things right: the theme, the stocks and the valuations.”







“The observation of investors steering deeper into Nvidia and the ‘magnificent seven’ may surprise some after fund selectors allocated \$2bn to the Xtrackers S&P 500 Equal Weight UCITS ETF (XDEW) in 2023 to downplay US large cap tech exposure.”

& Artificial Intelligence ETF (BOTZ), have opened the door for such elevated exposures, after the ETF’s top holding cap was raised from 20% to 35% last month to accommodate Nvidia’s growing footprint.

Elsewhere, some thematic strategies have far lower single stock thresholds. Lukas Ahnert, senior passive product specialist at DWS, said this highlights the ability of such ETFs to manage returns and risk concentration while remaining broadly invested.

However, Nvidia still makes its presence known within these ETFs. Between the start

of 2023 and late March this year, the stock comprised 31.7% of gains with a 9.6% weight in the VanEck Semiconductor UCITS ETF (SMH), 23.6% of gains with a 8.6% weight in the iShares MSCI Global Semiconductor UCITS ETF (SEMI) and even 16.9% of gains with just a 5.9% average weighting in the Xtrackers Artificial Intelligence & Big Data UCITS ETF (XAIX).

A similar story in sectors

While thematic ETFs have rightly or wrongly earned a reputation for concentration risk

and presenting unique challenges for index construction, Nvidia fanfare has also spread to more conventional corners of the ETF roster including sectors.

Unsurprisingly, a key focus for this discussion is US tech sector benchmarks which have dutifully tracked Nvidia’s rise in lockstep.

This is evidenced by the iShares S&P 500 Information Technology Sector UCITS ETF (IUIT) seeing its allocation to the stock hike from 4.6% to 17.6% within 15 months to the end of March and the Xtrackers MSCI USA Information Technology UCITSETF (XUTC) seeing its Nvidia weighting jump from 4.1% to 17.3% over the same period.

The chipmaker accounted for 27% and 25.1% of gains across the two ETFs, respectively, over that timeframe, even though both strategies are comprised of at least 65 constituents.

Perhaps more interesting is Nvidia’s journey to becoming a darling within ESG-screened tech sector strategies.



This is seen with the Amundi S&P Global Information Technology ESG UCITS ETF (WELU), which saw its Nvidia allocation triple from 7% to 21.3% and 32.4% of its gains owe to the chipmaker in the 15 months to March.

Similarly, an Invesco equivalent ETF tracking the same index saw its allocation to the chipmaker surge from 8.9% at launch in April last year to 19.2% by the end of March, playing a dominant role in the ETF's 92-strong basket.

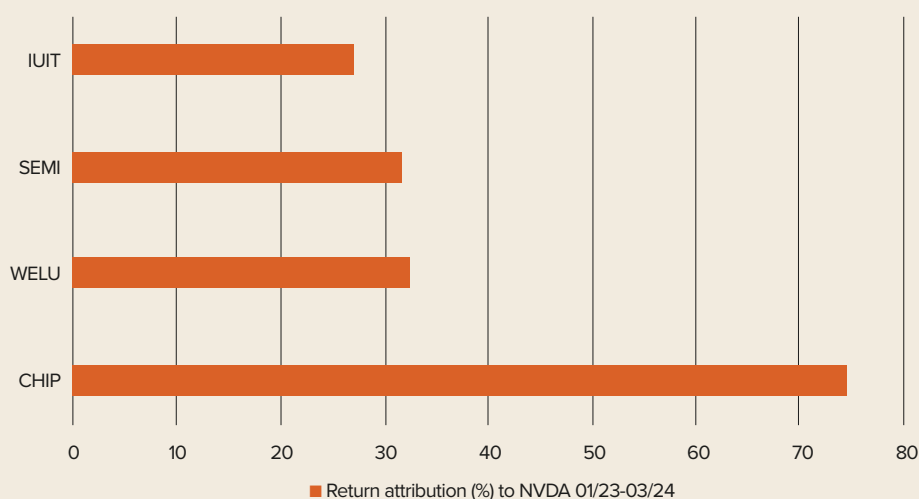
Should investors be concerned?

Examining Nvidia's rise to prominence across equity ETFs, Monika Calay, head of EMEA passive strategies research at Morningstar, suggested it is time for asset allocators to take note.

"The uptick in Nvidia weightings within thematic and sector ETFs is something we have noticed and it should be a material consideration for investors," Calay said.

However, the stock's recent tear has not

CHART 1: ETF RETURNS ATTRIBUTABLE TO NVIDIA



Source: Bloomberg, Amundi and BlackRock

mutated appetite for affected thematic ETFs. In fact, CHIP has welcomed \$101m inflows over the past 12 months – equivalent to a quarter of its total assets – and SMH, Europe's largest semiconductor ETF, has seen its assets under management (AUM) swell from \$1bn last June to \$1.8bn.

For those wishing to sidestep single stock concentration, Calay pointed to equal-weight thematic ETFs as a tool to avoid potential bubbles, but added this does not completely allay the risks of rules-based megatrend strategies.

"Investing in thematic funds is like placing a trifecta bet at the horse track," Calay argued. "You are trying to get three things right: the theme, the stocks and the valuations. Investors should be aware that much of their enthusiasm may already be priced in by the time thematic funds are brought to market."

Suggesting an alternative, Andrew Limberis, investment director at Omba Advisory & Investments, said active thematic ETFs would "make a lot of sense" in rotating between themes and individual holdings, but conceded "it is going to be a very difficult job to convince European investors".

In sector ETFs, a similar trend of performance chasing has played out in flows across strategies with high Nvidia exposure. BlackRock and DWS's US tech sector ETFs, for instance, received approximately \$700m inflows apiece between the turn of the year and 27 March, according to data from Bloomberg Intelligence.

"These tech ETFs are taking in a considerable amount of flows, relative to the risk-on sentiment we are seeing," Sebastian Cabral, research associate at Bloomberg Intelligence, said.

"There are still flows going into core S&P 500 ETFs, but what is also interesting is investors are getting more granular in their allocation to Nvidia and they are doing so via their exposure to these tech ETFs."

The observation of investors steering deeper into Nvidia and the 'magnificent seven' may surprise some after fund selectors allocated \$2bn to the Xtrackers S&P 500 Equal Weight UCITS ETF (XDEW) in 2023 to downplay US large cap tech exposure.

"It is interesting flows are still transferring into these products rather than steering on a more risk-averse basis," Cabral added.

Final word

Unlike past issues of small cap overconcentration and oversized stock ownership seen in thematic strategies, Nvidia's swarm across theme and sector ETFs is question for investors to answer from an asset allocation perspective, rather than a structural concern for the ETF wrapper.

As also seen in broad equity indices – where Nvidia has risen from 0.7% to 5.1% of S&P 500 products since 2020 – ETFs will continue to reflect the chipmaker's meteoric rise for as long as it continues.

Jamie Gordon is senior features reporter at ETF Stream

Beyond Beta

Investigating the smart beta, factor & ESG investment revolution

A 'volatile' situation

Analysing the low volatility UCITS ETF landscape

By Steven Goldin

At one point, low volatility and minimum variance ETFs were highly popular and supported by academic research that identified an anomaly in which low-risk stocks produced higher returns than high-risk stocks. This finding runs contrary to Modern Portfolio Theory and the Capital Asset Pricing Model.

One of the seminal papers identifying this anomaly was *Risk and the Rate of Return on Financial Assets: Some Old Wine in New Bottles* (Haugen and Heins, 1975). A follow up working paper written by Robert Haugen and Nardin Baker in 2012 included a comprehensive analysis of 21 developed markets and 12 emerging markets from 1990 to 2011 showing that stocks in the lowest volatility decile outperformed those in the highest volatility decile on a total return and risk-adjusted basis. This paper was no doubt welcomed by ETF issuers looking to launch and market low volatility-based ETFs.

Now it takes a 'volatile' situation for investors to become interested in low volatility strategies. Indeed, it was not until 2011, after the Global Financial Crisis, when ETF issuers began launching low volatility-based ETFs.

As for index providers, MSCI launched their first minimum volatility index in 2008 and S&P launched the S&P 500 Low Volatility index in 2011 and the US-listed Invesco ETF tracking this index now has a market

value of \$7.5 billion. Both indices have different methodologies but what they have in common is that they've underperformed the S&P 500 since their respective launch dates.

This is not an uncommon finding because relationships between factors including volatility, size, value, quality and momentum have a time-varying component resulting in relative performance being cyclical.

Certainly, low volatility stock ETFs can be a useful part of a dynamic asset allocation process, but it is helpful to understand the differences in their underlying methodologies and characteristics before investing and that's what the rest of this article sets out to do.

UCITS ETFs in our analysis

The ETFs included are listed in Chart 1 and were selected based on length of track record and to highlight different underlying index methodologies and fundamental variations (ESG, high dividend etc.).

Different methodologies and active risk

There are three main underlying index methodologies being employed across these six ETFs. The weighting methodologies have a big impact on the active sector exposures and ultimately tracking-error relative to a broadly diversified, market cap weighted benchmark like the S&P 500 (see Chart 2).

1. Low volatility indices use an inverse volatility weighting whereby stocks are ranked



based on their trailing volatility and those with a lower (higher) volatility receive a proportionally higher (lower) weighting. For example, the S&P 500 low volatility index only includes the 100 lowest volatility stocks. You are not getting a low volatility version of the S&P 500 but rather an exposure to the 100 least volatile stocks selected from the S&P 500. The MSCI low volatility indices take a more stratified approach to dampen the level of tracking error relative to the parent index.

2. Minimum volatility indices use a minimum-variance optimisation to determine the index composition and weights. Constraints are imposed at the security and

“The lowest tracking error ETFs use minimum-variance optimisation weighting with sector, security and factor constraints. The highest tracking error ETFs use inverse volatility weighting”



CHART 1: LOW AND MINIMUM VOLATILITY ETFs IN EUROPE

Ticker	Name	Assets (\$m)	Expense Ratio	Weighting Scheme
MVUS	iShares Edge S&P 500 Minimum Volatility UCITS ETF	\$2089.2	0.20%	Factor and min variance optimization
HDLG	Invesco S&P 500 High Dividend Low Volatility UCITS ETF	\$419.8	0.30%	Inverse volatility weighted
MVEA	iShares Edge MSCI USA Minimum Volatility ESG UCITS ETF	\$342.7	0.20%	Min variance optimization
USLV	SPDR S&P 500 Low Volatility UCITS ETF	\$135.4	0.35%	Inverse volatility weighted
UC95	UBS ETF (IE) Factor MSCI USA Low Volatility UCITS ETF	\$43.1	0.18%	Inverse volatility weighted
LUMV	Ossiam US Minimum Variance ESG NR UCITS ETF	\$38.5	0.65%	Min variance optimization

Source: Bloomberg at month-end February 2024

CHART 2: ACTIVE SECTOR WEIGHTS RELATIVE TO THE S&P 500 (EXCLUDING ETFs WITH ESG AND HIGH DIVIDEND FEATURES)

Sector	iShares Edge S&P 500 Minimum Volatility UCITS ETF	SPDR S&P 500 Low Volatility UCITS ETF	UBS ETF (IE) Factor MSCI USA Low Volatility UCITS ETF
Communication Services	-3.4	-7.2	-6.4
Consumer Discretionary	-1.7	-3.8	-6.5
Consumer Staples	4.3	16.5	10.0
Energy	-3.3	-1.8	-3.8
Financials	5.7	4.2	2.1
Health Care	5.6	-1.1	0.7
Industrials	-5.7	5.3	10.4
Information Technology	-5.2	-22.3	-25.1
Materials	-2.3	-0.30	1.0
Real Estate	1.5	-0.5	6.2
Utilities	4.6	11.0	11.5
Not classified	-0.0	0.3	-0.2

Source: Bloomberg at month-end February 2024

sector level to restrict the active level of risk versus a broad, market cap benchmark.

3. Minimum volatility with additional risk factor constraints. In addition to minimising variance, these indices include additional risk factor constraints as part of the optimisation objective function to control for market beta, size and style tilts. The result is a minimum variance ‘lite’ exposure with less active risk relative to the parent index.

Rolling 3-year annualised tracking error relative to the S&P 500

Tracking error has increased for all the ETFs as sector dispersion increased in recent

years. The lowest tracking error ETFs use minimum-variance optimisation weighting with sector, security and factor constraints. The highest tracking error ETFs use inverse volatility weighting and in the case of the Invesco ETF, also have a high dividend selection criterion (see Chart 3).

Rolling 3-year annualised Sharpe ratio

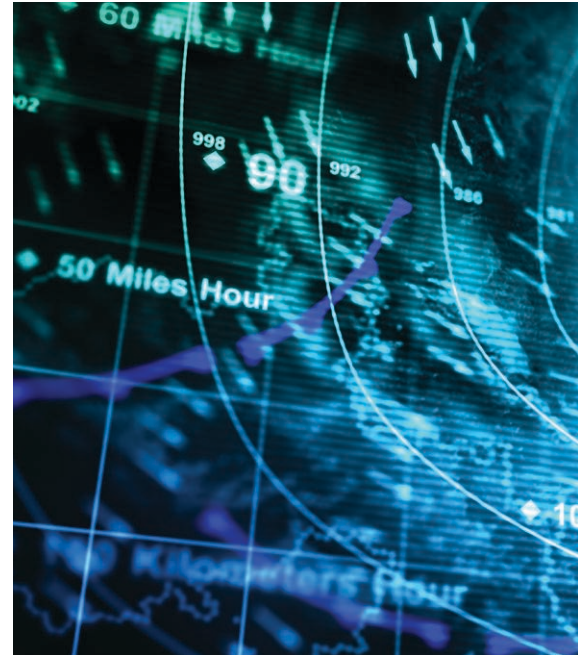
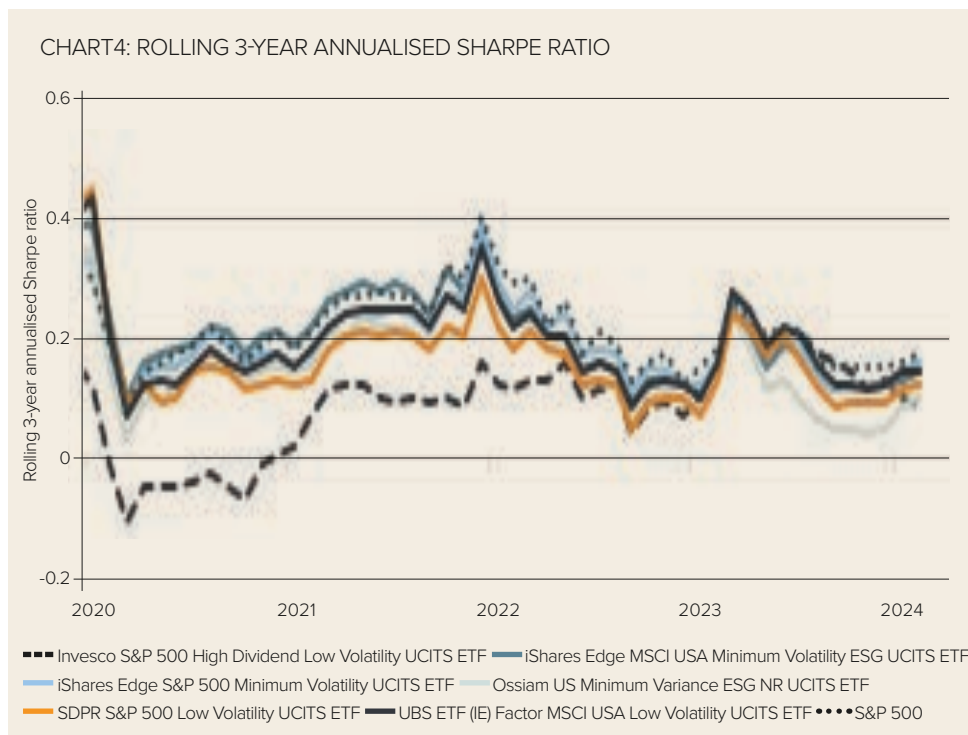
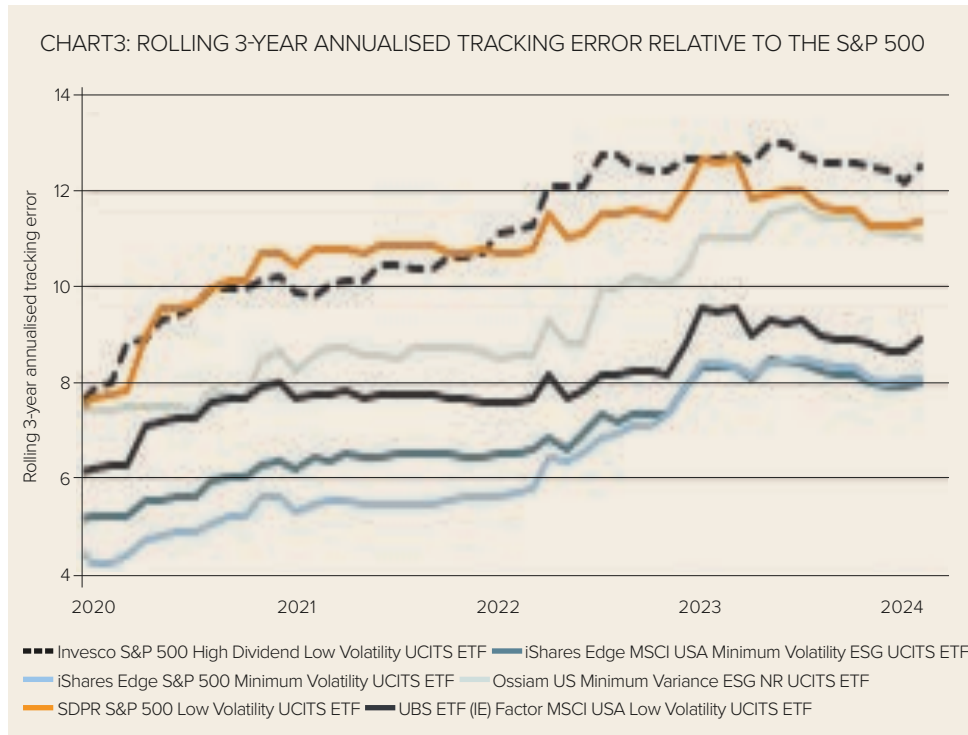
One of the characteristics of lower volatility indices is that they tend to deliver higher Sharpe ratios than the market index. For example, over rolling three-year periods going back to 1991, the MSCI USA Minimum Volatility index and S&P 500 Low Volatility

index had higher Sharpe ratios than the S&P 500 over 71% and 54% of rolling three-year periods, respectively. However, over more recent periods, this has not been the case for ETFs tracking these or similar indices as illustrated in Chart 4.

Long-term risk factor exposures of each low volatility focused ETF

A common characteristic of low volatility ETFs is a relatively low equity market beta. In Chart 5, the equity market betas range between 0.68 to 0.84 versus an S&P 500 market beta of 1.0. Additionally, all the ETFs have positive exposure to the value premium and unsurprisingly, the Invesco S&P 500

“Each ETF has an important residual component of its return which is independent to the risk factors but is correlated with the business cycle and may be due to differences in each ETF’s sector weights and security selection and weights within each sector”



high dividend low volatility has the highest exposure to the value premium.

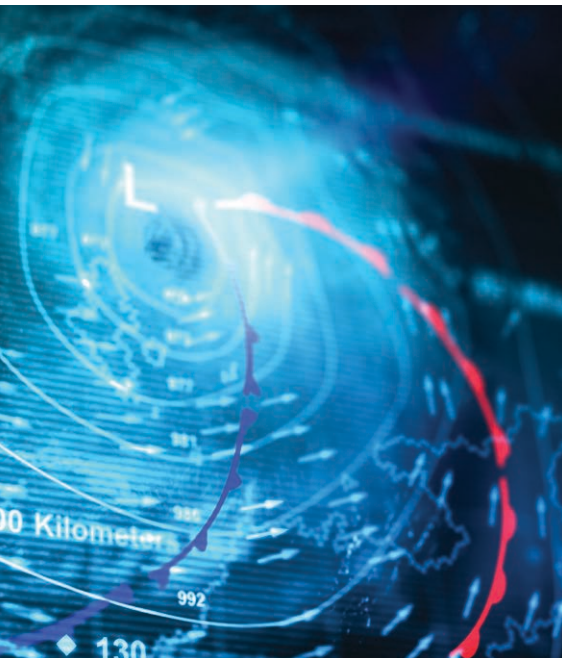
This ETF is the only ETF with a positive exposure to the small cap premium whereas the other ETFs have a negative exposure which means they have a large-cap bias. Lastly, the ETFs have very little momentum exposure. Collectively, this information is useful in understanding how these ETFs may fit into a portfolio and align with an investor’s risk profile and views on the market.

Low volatility factor ETFs returns are sensitivity to changes in business cycle variables

When evaluating the risk and return behaviour of these six low volatility based UCITS ETFs, Parala’s model captures not only each ETF’s exposure to four important risk factors including market beta, small cap, value and momentum risk premiums but also the fact that the performance of the risk factors themselves are sensitive to the business cycle.

Each ETF also has an important residual component of its return which is independent to the risk factors but is correlated with the business cycle and may be due to differences in each ETF’s sector weights and security selection and weights within each sector. We can identify these relationships using important macroeconomic variables like the default spread, term spread, short-term interest rate, dividend yield, VIX index and commodity prices.

Based on their sensitivities to these macroeconomic variables we gain additional in-



sights into their likely behaviour across the business cycle. For example, all the ETFs have a positive sensitivity to the default spread so if credit risk increases, these ETFs would be expected to benefit. Notice that that the Invesco S&P 500 High Dividend Low Volatility ETF has a positive sensitivity to the term spread whereas the iShares Edge S&P 500 Minimum Volatility ETF has a negative sensitivity.

In an environment where the term spread is inverting as we've experience recently, the iShares Edge S&P 500 Minimum Volatility ETF would be expected to perform better and that is indeed the case. The same would be expected in a rising rate environment which would benefit the iShares Edge S&P 500 Minimum Volatility ETF and weigh on the S&P 500 High Dividend Low Volatility ETF.

Overall, the current macroenvironment would appear to favour the iShares Edge MSCI USA Minimum Volatility ESG ETF and been least favourable for the Invesco S&P 500 High Dividend Low Volatility ETF and their relative performance seems to confirm this (see Chart 6).

Conclusion

It takes a 'volatile' situation for low volatility focused ETFs to show their merits which is why these ETFs may have lost some of their short-term appeal. In low volatility, strong economic environments, growth investing reigns supreme. However, low volatility focused ETFs may be useful to adjust sector, beta, volatility and macroeconomic diversi-

CHART 5: LONG-TERM RISK FACTOR EXPOSURES OF EACH LOW VOLATILITY FOCUSED ETF

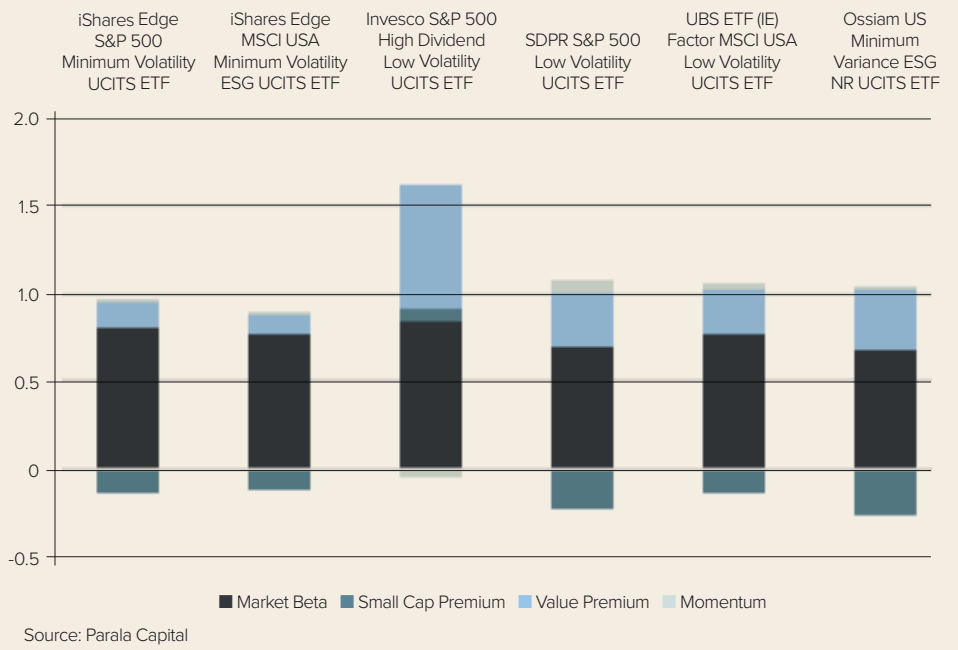
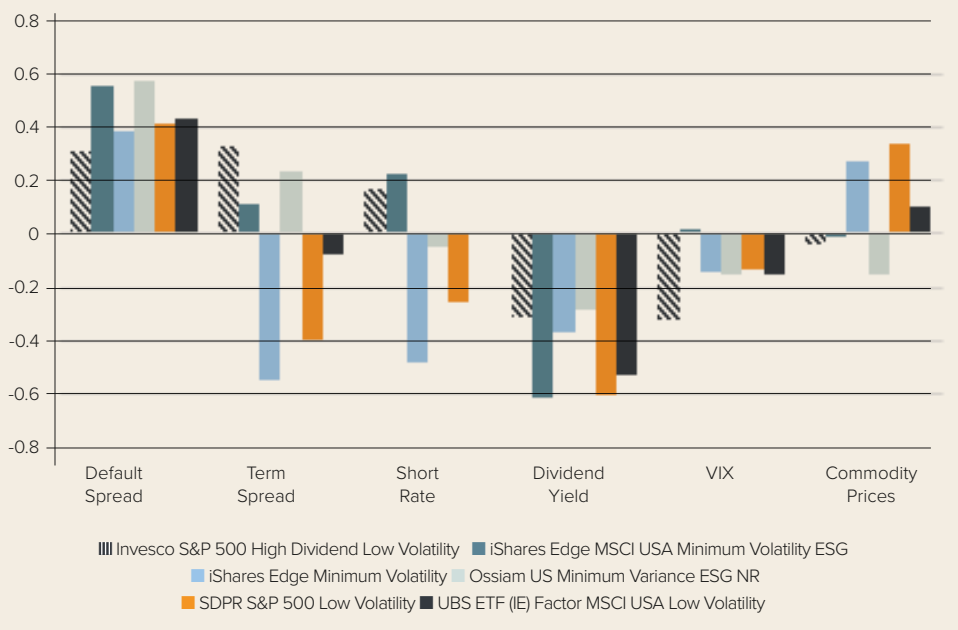


CHART 6: LOW VOLATILITY FACTOR ETFS RETURNS ARE SENSITIVITY TO CHANGES IN BUSINESS CYCLE VARIABLES



fication within a portfolio and for that reason represent a useful tool in the toolbox.

These low volatility UCITS employ different weighting methodologies, have different active sector, risk factor and macroeconomic exposures which can inform investors how they might behave in different market and macro environments.

Having a sophisticated model like Parala's may be helpful when making investment decisions but simply understanding each ETF's characteristics, risk factor exposures

and business cycle sensitivities can be useful to help professional investors select funds and build portfolios that align with their 'house' views.



Steven Goldin is managing partner at Parala Capital, which provides institutional investors and asset owners with asset allocation advice using advanced quantitative technology based on the academic research of its founding partners.

Events

This section provides a summary of the latest ETF Stream events including webinars, roundtables and the Big Call series



ETF Stream Presents

Crypto ETPs and innovation in the digital asset indexing space

Recent regulatory wins paint a brighter picture for crypto ETPs in Europe. With this momentum, will crypto indices continue to see single token domination, or will investors begin to look to more nascent basket indices?

Crypto has been stealing the headlines so far in 2024, most recently after the Financial Conduct Authority (FCA) paved the way for crypto exchange-traded product (ETP) listings in the UK for the first time.

With widening interest among professional investors looking to diversify their portfolios, questions are being asked about the future of this alternative asset in Europe and what innovations will be born out of increasing adoption.

Crypto indices present a particularly intriguing discussion. As single token indices continue to dominate the market, multi-token benchmarks start to emerge as an interesting alternative for investors looking to ensure diversification and avoid overweighting.

As a result, this roundtable, in partnership with MarketVector Indexes, assessed the growth of crypto ETPs in Europe, questions surrounding building and weighing a crypto index, regulatory developments and

Meet the experts



Bradley Duke
founder and chief strategy officer, ETC Group



Aaron Renkers
head of investments, VanEck Europe



Mandy Chiu
head of financial product development, 21Shares



Bruno Ramos de Sousa
head of US and Europe, Hashdex



James Butterfill
head of research, CoinShares



Martin Leinweber
digital asset product strategist, MarketVector Indexes

In association with



highlighting education as a key instrument to wider adoption across Europe.

Crypto ETP growth

Chiu: It took more than 30 years for ETFs to become mainstream. One of the main topics at a recent event I attended was active ETFs and less than 10 years ago people thought active ETFs were an odd idea, but now the industry has changed its mind. I am feeling quite hopeful about the evolution of crypto ETPs.

Renkers: More competition drives us all to do a better job and create better processes so new entrants into the market are a good thing. There is a lot that has been changing on the back end in terms of the infrastructure and it has become more mature. People are beginning to increasingly realise that these crypto ETPs are very robust products.

Leinweber: Over time basket solutions have become more in demand and I hope this will be an increasingly growing part of the cryp-

to future. They are more interesting than just having a plethora of single token indices. Currently, there are between \$50trn to \$60trn in global ETPs and multi-asset ETPs are between \$3bn and 4bn. So, it is still pretty small but I hope this will grow.

Duke: We had real challenges in the beginning. We could not find a bank that would open a bank account, they would close us down a few months later. Today, the regulatory environment is so much better and the Markets in Crypto Assets Regulation (MiCA) is a very decent piece of bass regulation. The statistics bear out that even though crypto ETPs have always been driven by retail, there are still a lot of retail investors that have yet to touch it.

Ramos de Sousa: The interesting segment of the market is the index part. That is how [Hashdex] started and the focus has always been on the indices and the market will slowly mature towards this. Hopefully, those moving into the space have a long-term

commitment to the asset class rather than it just being another product on the shelf.

Building crypto indices

Leinweber: Any index out there is based on an algorithm which means it adopts a systematic approach. You often see crypto enthusiasts chasing narratives, but what is more important to focus on is the crypto market return. If you can capture the top 10 to 25 cryptocurrencies with a cap-weighted approach and you rebalance it regularly, then it is a set-and-forget strategy. It is something you can allocate to without worrying about picking the right coin. You can have a systematic approach if you cap-weight your indices, buying the winners and then selling the losers over time.

Butterfill: Historically, some of the most successful equity markets tech funds have been equal-weighted and quite often they are agnostic on a particular company but like a particular theme or style. Those have been the most successful in the equity markets, however, that is not been the case in the crypto markets yet.

Chiu: Investing in cryptocurrencies is a kind of thematic investment and there are various ways of building thematic portfolios. You can equally-weight them or apply some sort of capping but it depends on what the investors are looking for. If they just want something to represent the market then maybe just tell them to buy bitcoin and ethereum. However,

“If you can capture the top 10 to 25 cryptocurrencies with a cap-weighted approach and you rebalance it regularly... It is something you can allocate to without worrying about picking the right coin”

Martin Leinweber, MarketVector Indexes



“Commercially, you must consider whether there is a valid investment rationale for owning this particular cryptocurrency. Clients are increasingly asking that question”

James Butterfill, CoinShares

an investor could want to invest in a diversified pool of digital assets and therefore would like to see who the winners are, maybe top five, 10 or 20.

Ramos de Sousa: [Hashdex] has never built top 10 or top 20 products because it does not represent the market. If the index is dynamic, you should be able to reflect that if today it is seven, next quarter it is 15 and in the following one back to 18 that should show where the market is going.

Regulation

Leinweber: When looking at Europe, you have around 20 tokens that are approved by BaFin and other European regulators, but we see Switzerland is opening up. The Swiss exchange will come with new rules on 1 April that could create a universe of 38 tokens. We screened our top 100 index and suddenly you have a token available which opens the door for interesting sectors.

Butterfill: It is easy to get into the trap of being an issuer and thinking that it is the next big thing but then six months to a year down

the line no one is buying it. Commercially, you must consider whether there is a valid investment rationale for owning this particular cryptocurrency. Clients are increasingly asking that question.

Duke: I think all issuers have grappled with this problem as well. The exchanges are only one side of it. One of the problems is that you are dealing with a lot of these coins that are meme coins which carry a lot of regulatory risk, you do not know what is going to happen or if there are going to be issues with them, and you do not want to be associated with that.

Chiu: The vetting process is quite important. At 21Shares, we have got requests from our investors who come with a lot of money and there are times when I had to turn them down because we said we cannot launch a product like this. It is a hard decision but striking a balance is very important. However, being in the industry long enough means that we are better at the vetting process.

Renkers: For the smaller coins, it is more important to look at your selection rules. From

the ETF world, we all know the benefits of having a basket, but for crypto ETPs, that still does not resonate.

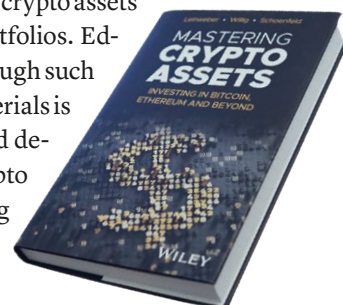
Education key to adoption

Duke: The reality is that the education is just not there with crypto. There is a lot of sexy innovation that is going on. But really when you speak to investors, you go to the coalface and they are only talking about bitcoin.

Ramos de Sousa: New entrants into the crypto market need to be committed to getting the education out there and not just pushing a product. There is work that the media should do, aside from just key crypto players, to understand why there is value in a currency that does not depend on central banks.

Butterfill: The interest outside of bitcoin can wain very quickly and the knowledge levels vary hugely. I saw an asset manager here in the UK, and they are still getting their heads around bitcoin’s limited supply, which are simple questions.

Leinweber: Furthermore, to support this educational push, I recommend interested parties consult resources like our book, *Mastering Crypto Assets*, which offers a deeper dive into integrating crypto assets with traditional portfolios. Educating oneself through such comprehensive materials is a crucial step toward demystifying the crypto space and leveraging its potential for portfolio diversification.





KEY TAKEAWAYS

Renkers: We have talked a lot about baskets. It is going to happen but probably not as quickly as people might think. We should also see bitcoin dominance go down a little bit.

Butterfill: We have a fund manager survey where we ask clients what they think are the key risks and regulation and government bans are still right at the top. Maybe that will change as this was taken as a snapshot from January.

Chiu: I would say regulatory ambiguity

put off a lot of players that could have contributed massively to the ecosystem. That does not help people with their experience of their first crypto ETP investment, because there is a lack of competition. The development in the US is really interesting to watch because the growth will have a ripple effect in Europe.

Duke: As the market becomes more sophisticated the types of products will become more sophisticated, using derivatives as a way of boosting performance or offering a defined outcome which will come with maturity.

Ramos de Sousa: On the regulatory risks, the bitcoin ETF in the US was a clear win for the industry. Sometimes people attribute the key moment to the BlackRock filing for application, but it was not the filing that made the difference, it was the lawsuit.

Leinweber: On our end, I am less concerned about regulatory risks. The primary uses of cryptocurrencies are still heavily influenced by speculation. We understand bitcoin's role as a store of value, but it is crucial to identify and articulate other compelling use cases. Determining these 'killer applications' remains my top priority.



ETF Stream Presents

ETFs to address asset allocation challenges in a new market regime

Overconcentration and interest rates are weighing heavily on investors' minds, driving core asset allocation decisions. How are investors addressing this through ETFs?

Chair: Tom Eckett, editor at ETF Stream

With a new market regime upon us fund selectors are increasingly turning to ETFs to address asset allocation challenges. Market overconcentration is a key concern, while sticky inflation and the

prospect of fewer rate cuts by the Federal Reserve throughout 2024 are resulting in investor caution.

It has also led to a delay in the 'bonds are back' narrative, with fund selectors wary about adding duration to their portfolios.

ETFs can play a key role in overcoming these challenges, allowing investors to be more granular in their asset allocation decisions in a bid to take advantage of market dispersion. Investors that choose to use the full ETF toolbox will find many ways to construct their portfolios, be it through thematic, ESG or the rapidly growing active ETF space.

Cryptocurrency exchange-traded products (ETPs) is another area investors are increasingly considering adding to their portfolios, however, challenges around accurately valuing digital assets such as bitcoin remain a stumbling block.

Market outlook

Mitchinson: This time last year our macro team would have been telling you we were going to have a hard landing. Suddenly that scenario has disappeared and we have gone through a period where we have priced in no landing at all. Two things people are not looking at is what if the US does fall off a cliff and Europe becomes stagnant.

García: Despite the recent inflation readings in the US, we have not seen the market fall thanks to the robustness of the US economy (employment, consumer demand and earnings growth) and the dovish narrative

Meet the experts



José María de Cendra Núñez-Iglesias
corporate investment banking
mercados, Santander



Juan Hernando
director of advisory,
Mora Wealth



Stacie Mitchinson
systematic investment director,
Fidelity International



Patricia Pomares
portfolio manager and
senior analyst, Caixabank
Asset Management



Alberto García
head of asset allocation,
ACCI Capital Investments



Domingo Barroso
ETF sales director for Iberia,
Fidelity International



Vicente López Quetglas
portfolio manager and
senior analyst, Bankinter
Asset Management



Miguel Lopez
investment analyst,
Varianza

In association with



from the Fed. I am positive about the US over the medium term and anticipate the Fed to cut rates from June. Europe is a different story, as economy is weaker, but you can take advantage of some undervalued sectors like financials.

Lopez: There is more political risk ahead and inflation in the US could be stickier because of growing geopolitical tensions coming out of an eventual Donald Trump return. I can see the soft to no landing arguments as long as consumption and labour markets stay strong and there is no credit event. However, there is some data we should be concerned about, including the inverted yield curve, saving levels and sticky inflation.

Quetglas: We are neutral in several asset classes and it is a question of dispersion.

There is pressure on growth, Europe is doing nothing right now, the US is improving but you have massive dispersion in the market. We have started to allocate to China, they do have problems but you are starting to see light at the end of the tunnel.

Hernando: We have a soft landing as our central scenario. The European Central Bank (ECB) is wary of cutting rates too soon. The question for us is around overconcentration and we are fighting against that in portfolios, there is a fear of being out of the market. Neutrality is a way to structure your portfolios in this scenario.

Barroso: There is also the peak reversion story. We have a lot of asset classes, markets and indices at an all-time high but what are the key drivers? Are we losing any opportu-

nities and will we see a peak reversal or will momentum continue to drive the market?

Fixed income

Hernando: After so many years fixed income is back. Last year was a bit tough, especially in fixed income when we were expecting a bounce back which did not come until November and December. We have around a three or four-year duration in our fixed income portfolio.

Barroso: The question for investors is are they favouring taking more credit risk or are they more conservative at the moment?

López Quetglas: We like the asset class but we do not see it as a massive opportunity at the moment. We are trying to move away from duration, which is less than four years, but the question is where do we see interest rates going? In the beginning, we were more on the credit side and less aggressive high yield.

Lopez: We are more on the conservative side of fixed income regarding interest rates and we are not comfortable with increasing duration dramatically because still see inflation being sticky. On the financial side, we like subordinated debt, avoiding the Swiss ones due to regulatory issues. In corporate bonds, we prefer non-cyclical sectors.

“I am positive about the US over the medium term and anticipate the Fed to cut rates from June. Europe is a different story, as economy is weaker, but you can take advantage of some undervalued sectors like financials.”

Alberto García, ACCI Capital Investments



“We have been monitoring crypto for a couple of years and it acted as protection during some downturns, but there has also been some shocks and we do not want to include them in our portfolios yet”

Miguel Lopez, Varianza

Mitchinson: Our products are not taking any bets on duration. We use an in-house multi-factor approach designed by the quant team which can implement a client’s view through an ETF.

We have sentiment, valuation and fundamental buckets which we create using around 200 data points to generate a credit factor.

Cryptocurrencies

Barroso: We are really supportive of digital assets. There is a fever in the market at the moment for the adoption of digital assets in investor portfolios and we have seen an uptick institutionally. We are seeing asset managers in Spain launch a group of funds which involve digital assets, so there is a lot of space to include it as an asset class.

Hernando: The environment is supportive but we do not invest in bitcoin at the moment. Valuing it is a challenge, flows are coming to the market but will come to a halt at some point.

García: There are a lot of question marks around the asset class. It is very complicated measure the future risk-return profile and how much the price is being driven by the demand and supply of retail or institutional investors. There is an opportunity and we would like to use a very small amount in our portfolios to have some uncorrelated alpha to the index, always risk adjusted.

Lopez: We have been monitoring crypto for a couple of years and it acted as protection during some downturns, but there has also been some shocks and we do not want to include them in our portfolios yet. We are willing to take a look and stay informed, but we are sceptical about the 5% allocation argument based on its market cap.

López Quetglas: We are monitoring but not investing in digital assets. In terms of valuation, nobody is modelling it correctly. I prefer to look at bitcoin as a new way of doing things, all major banks are looking at it and working on things such as blockchain for its speed and security.

Active ETFs

Mitchinson: The beauty of active ETFs is they can deliver alpha at low cost and low tracking error. It gives investors more choice versus an index. It is the idea you can outsource that choice to somebody else by being active versus the core benchmark.

Hernando: It is something we would consider looking at. We have not been very familiar with active ETFs but certainly want to learn more about them.

López Quetglas: I see two different trends on the active side. One is to take the normal standard index and take positions on either side. Now I am seeing experts building the index for me, but these have nothing to do with passive management. We invest in a mix of passive and active, but at the beginning it was very hard to find an active fund for our thematic exposures.

Lopez: We are a mix of active and passives. Whenever we looked at inefficiencies we use active to give us a factor, conservative or aggressive bias. We use passive ETFs to get quick exposure to some sectors and when we gain more knowledge in certain sectors we change to a direct investment.



García: I would like to use active funds to take advantage of inefficiencies in less liquid assets like credit or emerging markets. Overall, I am quite happy with passive funds, as the current ETF universe allows us to create diversified portfolios with the return-risk profile we look for.

“We are really supportive of digital assets. There is a fever in the market at the moment for the adoption of digital assets in investor portfolios and we have seen an uptick institutionally”

Domingo Barroso, Fidelity International



Data dashboard: March 2024

Gold, silver and copper miner ETFs were among the best-performing ETFs in March as commodity prices continued their strong start to 2024

Data provided by



Data as at 21 March

TOP PERFORMANCE

Ticker Return

TOP 10 BEST PERFORMING ETFs

Sprott Copper Miners ESG-Screened	ASWD	14.93
Global X Copper Miners	GOFC	14.43
iShares Copper Miners	MINE	13.36
Vaneck Junior Gold Miners	GJGB	12.18
UBS ETF (CH) - Silver (USD) A-Dis	SVUSA	11.90
L&G Gold Mining	AUCP	11.89
UBS ETF Solactive Global Pure Gold Miners	GGMUZ	11.32
Amundi NYSE Arca Gold Bugs	GD91	11.01
iShares Gold Producers	SPGP	10.90
Global X Silver Miners	SILG	10.89

TOP 10 WORST PERFORMING ETFs

Electric Vehicle Charging Infrastructure	ELEP	-9.02
Global X Genomics & Biotechnology	GNDM	-6.79
First Trust Nasdaq Clean Edge Green Energy	QCLN	-5.74
WisdomTree Biorevolution	WBIO	-4.32
WisdomTree Cybersecurity	WCBR	-3.38
VanEck Rare Earth and Strategic Metals	VVMX	-3.31
HSBC S&P India Tech	HSPX	-3.28
Xtrackers MSCI Europe Consumer Staples ESG Screened	DXSK	-2.99
Global X Hydrogen	HYGG	-2.82
Xtrackers MSCI Africa Top 50 Swap	XMAF	-2.73

INFLOWS

OUTFLOWS

Name	Ticker	Inflows (\$m)
iShares Core S&P 500	CSPX	1,169.19
iShares Core MSCI World	SWDA	882.34
Invesco Msci USA ESG Universal Screened	ESGU	721.84
HSBC S&P 500	HSPX	544.06
iShares MSCI USA ESG Enhanced UCITS ETF USD (DIST)	EEDS	521.76
iShares MSCI EM ESG Enhanced UCITS ETF USD (ACC)	EDG2	476.24
Invesco S&P 500	SPXP	437.93
SPDR S&P 500	SPY5	394.30
Amundi MSCI Japan	LCUJ	375.10
Xtrackers II EUR Overnight Rate Swap	DBXT	372.30

Name	Ticker	Outflows (\$m)
iShares Core € Corp Bond	IEAC	-1,164.51
iShares MSCI USA SRI	SUAS	-1,075.94
iShares J.P. Morgan EM Local Govt Bond	SEML	-927.86
Amundi US Curve Steepening 2-10y	STPU	-485.51
iShares \$ Corp Bond UCI	LQDE	-415.26
Amundi MSCI USA SRI Climate Net Zero Ambition PAB	USRIN	-391.61
Ossiam ESG Low Carbon Shiller Barclays Cape® US Sector	5HEP	-351.17
AMUNDI S&P 500 ESG	S500	-316.17
DEKA MSCI EUROPE CLIMATE CHANGE ESG	D6RR	-268.64
SPDR MSCI EUROPE HEALTH CARE UCITS ETF	HLTH	-262.09

NEW LISTINGS

Name	Fund ISIN	Name	Fund ISIN
Amundi Euro Stoxx Select Dividend 30	C051GY	Figment Ethereum Plus Staking Rewards ETP	ETHFSW
Leonteq ETP on Adaptivv Downside Control US Tech Idx	ADTICBW	Figment Solana Plus Staking Rewards ETP	SOLFSW
iShares Core MSCI Europe	CEBZGY	UBS (IRL) ETF PLC - MSCI World	WORLD SW
UBS ETF MSCI Canada ESG Universal LCS	CAESG SW	Leonteq ETP on Leonteq Bitcoin ETF Index	BTCL SW
UBS ETF EUR Ultra-Short Bond ESG	SHORT IM	SPDR® Bloomberg 0-3 Year Euro Corporate Bond GBP Hedged (Acc)	SEGHX I2
UBS ETF S&P 500 Climate Transition ESG	CT500 SW	SPDR® Bloomberg 0-3 Year Euro Corporate Bond USD Hedged (Acc)	SEHAX I2
UBS ETF S&P 500 Climate Transition ESG (Hedged To EUR)	BCFGGY	SPDR® Bloomberg 0-3 Year Euro Corporate Bond USD Hedged (Dist)	SEHDX I2
UBS ETF S&P 500 Climate Transition ESG (Hedged To GBP)	CT5GLN	SPDR® Bloomberg 0-3 Year Euro Corporate Bond (Acc)	SEUA GY
HSBC FTSE EPRA NAREIT Dev Climate Paris Aligned (Acc)	HPNALN	1valour Stoxx Bitcoin Suisse Digital Asset Blue Chip	BCIX GY
HSBC FTSE EPRA NAREIT Dev Climate Paris Aligned (Dist)	HPEDLN	Xtrackers MSCI World ex USA	EXUS GY
Amundi MSCI World Uci Etf - Eur (D)	EWLDFP	Leonteq ETP on BX Swiss Top 30 Index	TOP30 SW
Cardano ADA Staking by Liqwid ETP	CASLCHFSW	UBS ETF MSCI EM ex China Socially Responsible	EMXCNS SW



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