

## Future development of the European ETF/ETP landscape



*Noticeable differences between Europe and the US concerning the prospects in terms of Assets under Management and number.*

Guest article by Sushil Krishnan, ETFs & Flow Derivatives Sales, UniCredit

In the ongoing discussion on the prospects of the European ETF landscape in terms of Assets under Management (AuM) and number of listed products it is necessary to distinguish between Europe and the US. From an economical and geographical perspective the US are fully integrated with approx. 311mn inhabitants<sup>1</sup> while the European continent consists of 45 sovereign states with a partial monetary union, some economical regulations and 739mn inhabitants<sup>2</sup>. The latter named are only examples as you can find a plenty of them to describe the economical, structural and cultural differences between the US and Europe. In terms of ETFs and ETPs it has to be born in mind that almost every European capital has its own exchange which dominates the trading activity in the respective home market (e.g. SIX Swiss Exchange in Switzerland, NYSE Euronext Paris in France, etc.) whereas in the US only three exchange places are dominating almost the whole market (NYSE Arca [NYSE] for cash-based products<sup>3</sup>, Chicago Board of Trade [CBOT] for equity derivatives and Commodity Exchange [COMEX or CME] for commodities and commodity derivatives). Hence, most of trading volume and market participants are concentrated which leads ultimately to tighter spreads and higher competition between market maker and issuers. Additionally, the legal framework for ETPs in Europe is different from the one in the US. In order to be able to access the full range of financial products in the USA one has to be a professional investor. The rules from the U.S. Securities and Exchange Commission (SEC) on information requirements and prospectuses (and liability concerning information contained in brochures) are much stricter when the product will be offered to private investors. Thus, private investors are very limited in the variety of products as the investor will need high margins for derivatives or will not be allowed to buy privately placed products like notes due to being not classified as a professional investor<sup>4</sup>. This

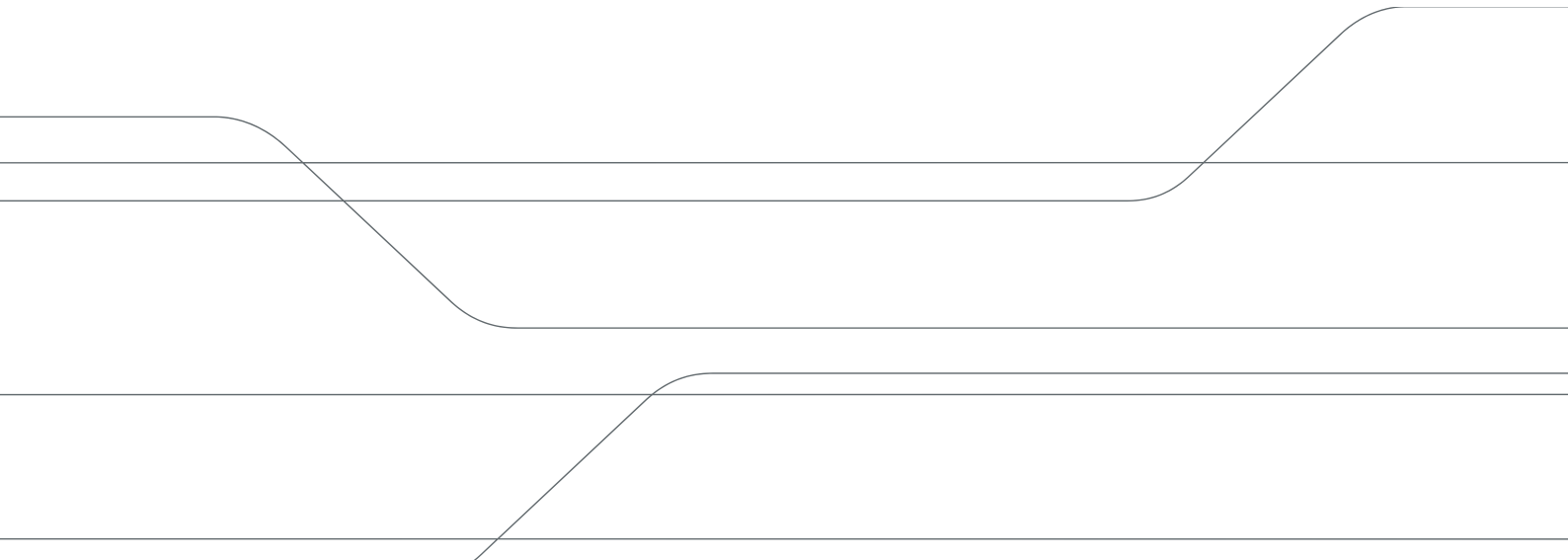
brings us to a crucial point when comparing an US investor with one from Europe: In the US investors are much more limited by the number of products than their European equivalents. Once the ETFs were invented, private investors were able to easily get exposure to complex structures, short- and leverage exposure within their portfolios without facing those difficulties.

#### **Fragmentation offering opportunities**

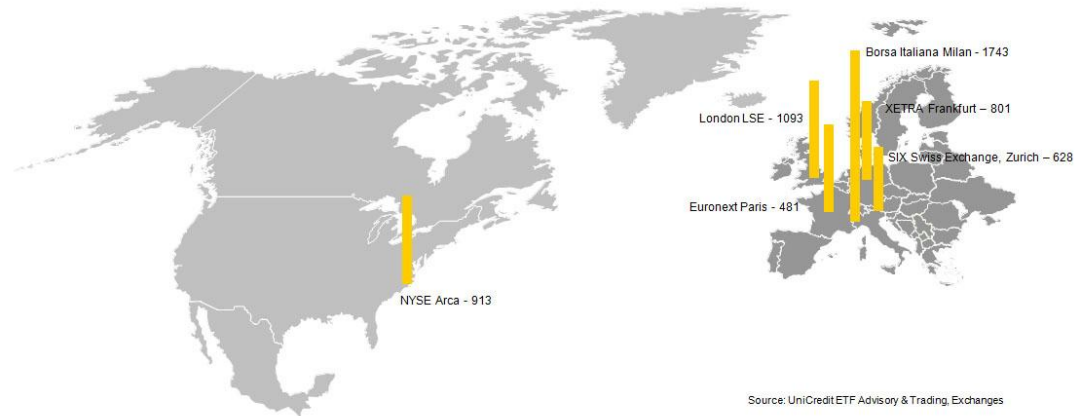
From the above we can draw two main conclusions – the local predominance of the European exchanges in their home markets leads to a fragmentation of the listed products across Europe (Swiss investors prefer to buy a SMI ETF on SIX Swiss Exchange, as a German investor will buy a DAX ETF on Frankfurt/XETRA)<sup>5</sup> and finally to lower turnover and wider spreads against the case of only one exchange and one product (almost every European exchange has an own Euro STOXX 50 ETF and several cross listings although it is a Pan-European product). In contrast, in the US there is only one exchange which dominates the ETF market. On the other hand, in Europe niche products and new issuers can enter the market easier as they can gather market share by listing products on several exchanges and do not have to compete the market leaders in the first step. This can be seen on the example of the Euro STOXX 50<sup>6</sup> as there are more than 20 products listed in on more than 15 exchanges so far. In Europe there are more than 1,070 ETFs/ETCs with more than 3,700 cross listings<sup>7</sup> – both exceeding the numbers from the US ETF market, but still lagging behind the assets under management.

#### **Where will the European ETF/ETP market head?**

We came to the conclusion, that the European ETP market will grow further massively, in the number of products, issuers and AuM. Contrary we do see the developments in the US where we observe a stagnation of products (new listings and delistings are setting the other off). In our opinion the absolute numbers of products and issuers will double in the next three years (only in the last six months there were approx. 250 products issued) before a consolidation on the issuer side and consequent delisting of unprofitable/ too small funds will begin. A lot of issuers are very well capitalised and waiting for the right moment to acquire closed down business of others. But this is only possible when there are any issuers willing to sell their business. Finally, it is always the investor who decides which business will be profitable, as every fund can only be profitable at a certain level of Assets under Management.



## Number of listed products in Europe and US exemplarily



<sup>1</sup> <http://www.census.gov/main/www/popclock.html> - March 22nd 2011.

<sup>2</sup> See 2011 data report of «Deutsches Institut für Weltbevölkerung».

<sup>3</sup> Products like equities, certificates, notes and ETFs/ETCs.

<sup>4</sup> See United States of America Securities Act from 1933.

<sup>5</sup> See chart «Number of listed products in Europe and US exemplarily».

<sup>6</sup> The 50 largest companies denominated in EUR and evaluated by free-float market capitalisation.

<sup>7</sup> Listings of the same fund on a different exchange than the primary listings.

<sup>8</sup> See UniCredit Delta One Navigator, 1. Quarter 2011.

### The Author

Sushil Krishan joined HVB/UniCredit in 2004. In 2009 he started at the ETF & Flow Derivatives Sales Team and advises European Investors regarding the ETF market. Prior Sushil worked with HVB/UniCredit's Equity Capital Markets and Corporate Fixed Income Derivatives Team. Sushil holds a B.Sc. in Finance from Frankfurt School.

In 2001 HVB/UniCredit issued the first ETFs in Europe under the brand IndEXchange before selling the issuing business in 2007. Today UniCredit's ETF Advisory & Trading Team provides liquidity to the nine largest European exchanges in more than 600 ETFs, offers OTC prices on every ETP globally and advises clients around the ETP space.

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