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# Strategic Beta ETPs



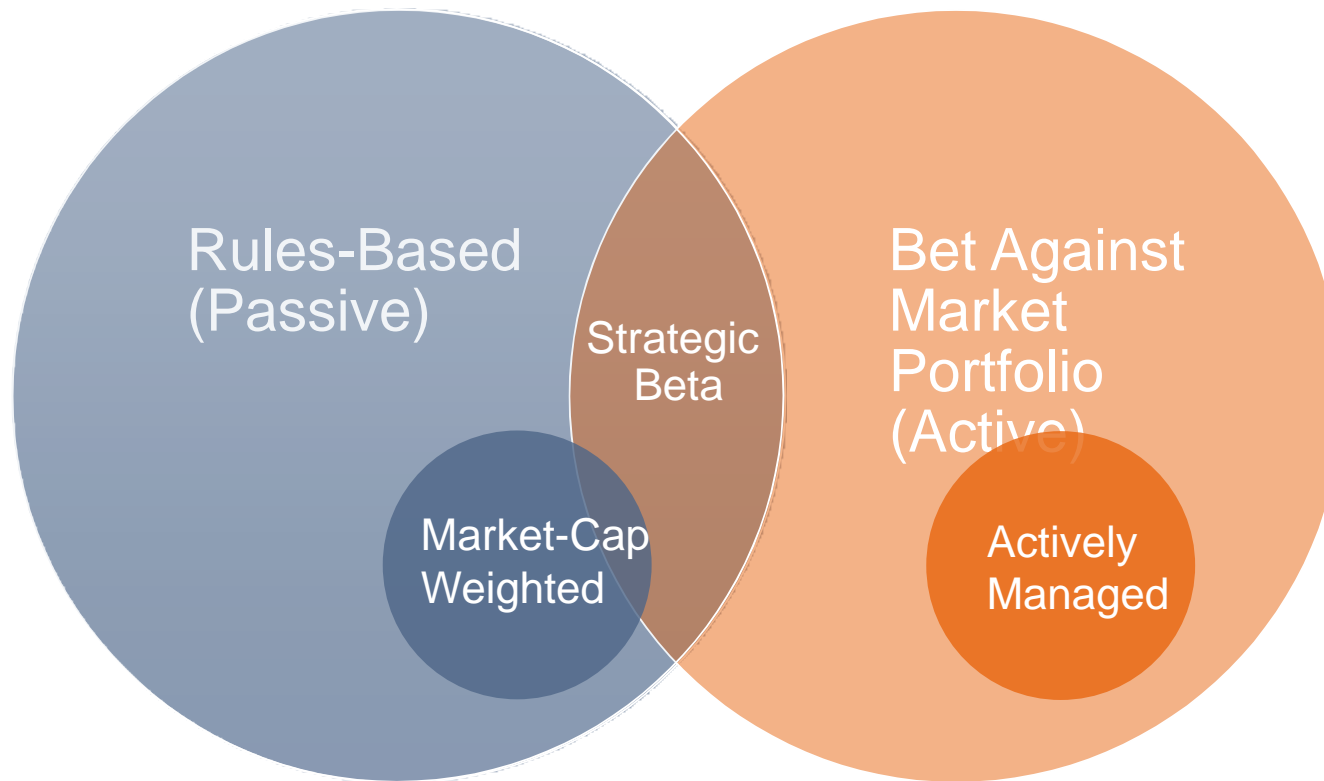
Ali Masarwah  
Editorial Director – EMEA

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Assets are flowing into passive investment vehicles that are increasingly active in their nature and implementation—the line between active and passive is now more blurred than ever before

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## Is Strategic Beta Passive, Active, or Both?



# Morningstar's Strategic Beta Taxonomy



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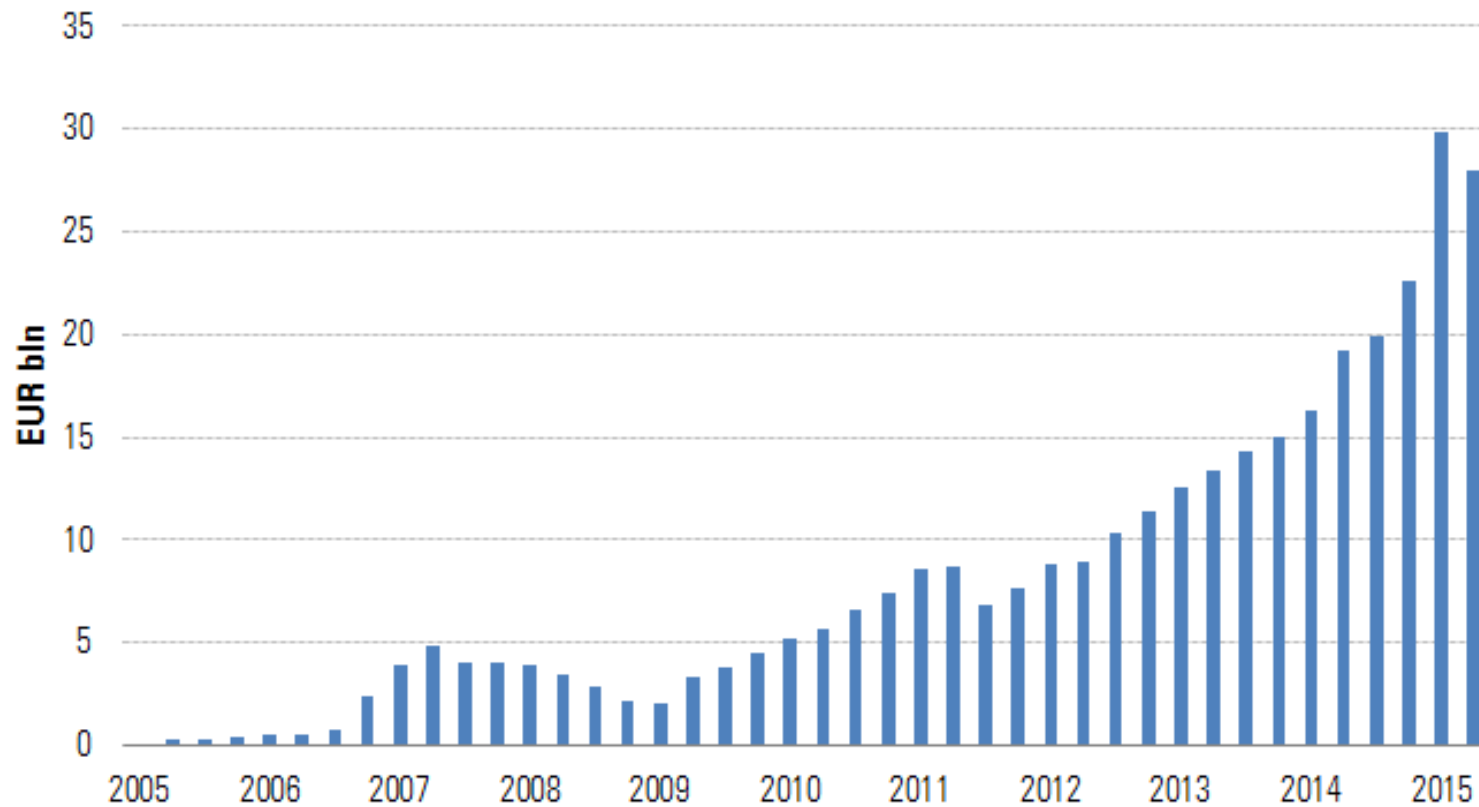
## What's Driving this Trend?

- ▶ Investors cite multiple reasons for using strategic beta products
  - ▶ Managing risk
  - ▶ Enhancing returns
  - ▶ Tactically adjusting asset allocations
  - ▶ Portfolio completion
  - ▶ Reducing fees
  - ▶ A general disillusionment with active managers

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## Strategic Beta AUM Growth in Europe Outpaces Broad ETP Market

### Strategic Beta ETP AUM - Europe

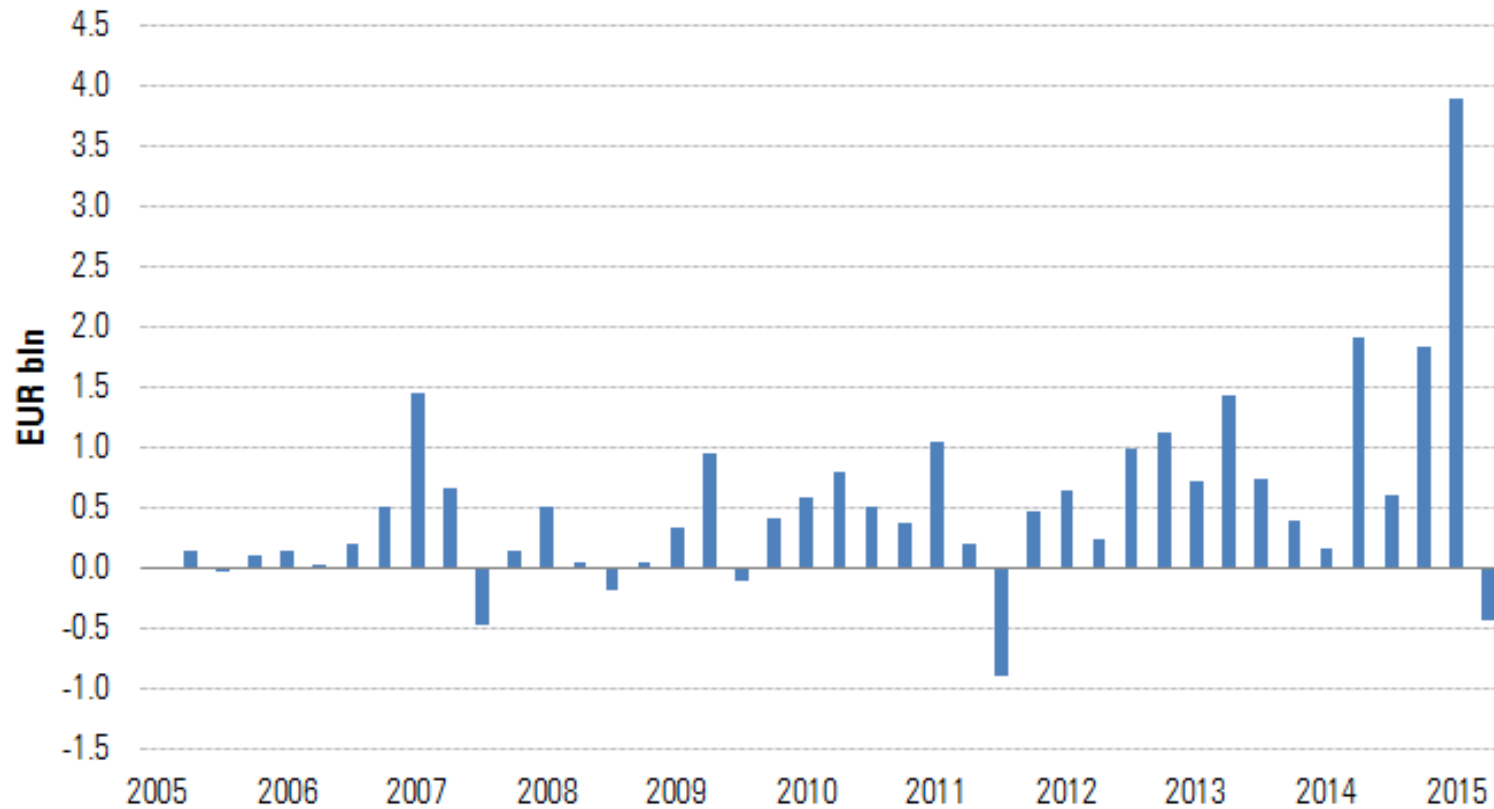


Source: Morningstar. Data as of 30 June 2015

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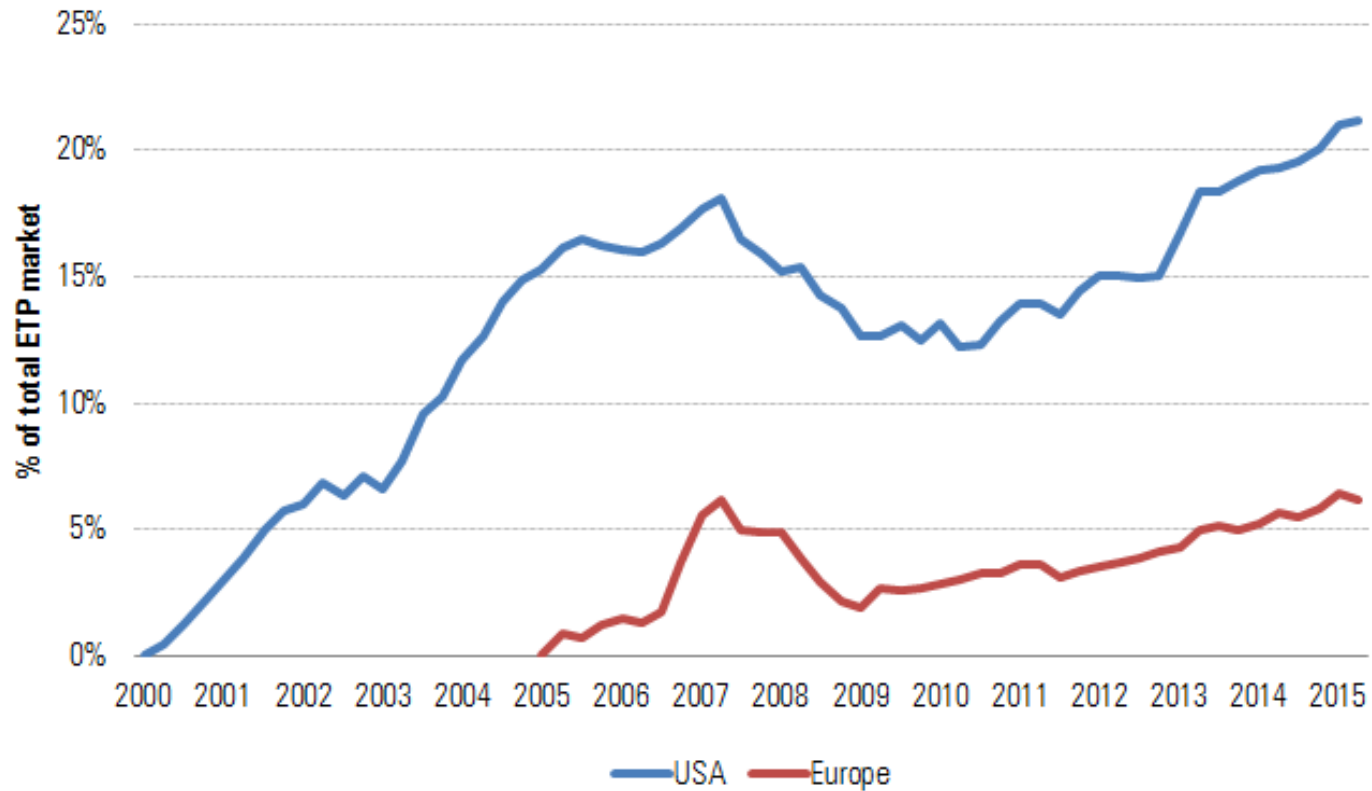
## Growth Has Been Driven by Net New Cash Flows

### Strategic Beta ETP Net Flows - Europe



Source: Morningstar. Data as of 30 June 2015

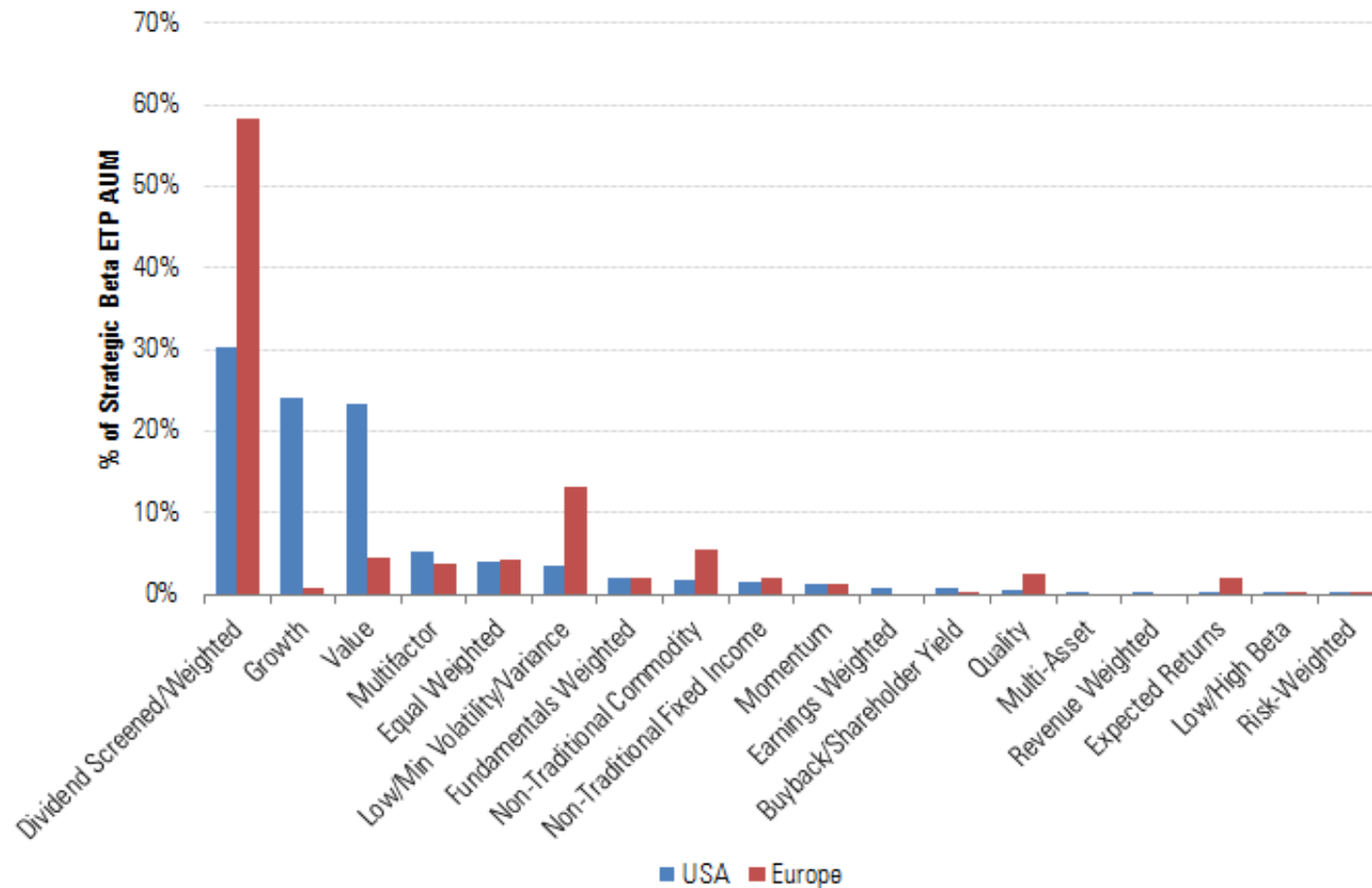
## Evolution of Strategic Beta ETP Market Share – US v Europe



Source: Morningstar. Data as of 30 June 2015



## US v Europe – Favoured Strategies



Source: Morningstar. Data as of 30 June 2015

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## How to Select Strategic Beta ETPs

- × Low cost
- × Low assets in relation to estimated capacity
- × Efficient exposure
- × Capable sponsor—indexing skill matters

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## Morningstar's Mission

- ▶ The goal of Morningstar's research team is to play the role of referee in this space
  - ▶ By laying the ground rules
  - ▶ Highlighting the winners
  - ▶ Calling out the losers
  - ▶ All in the interest of helping investors navigate this increasingly complex landscape

## Strategic Beta ETPs in Morningstar Direct – Data Points & Flows

<input type="checkbox"/>	Name	Strategic Beta	Strategic Beta Group	Strategic Beta Attributes	Prospectus Net Expense Ratio	Primary Prospectus Benchmark
<input type="checkbox"/>	1 iShares Developed Markets Property Yld	Yes	Return Orie	Dividend Screened/Weighted	0.5900	FTSE EPRA/NAREIT Dev Dividend
<input type="checkbox"/>	2 SPDR® S&P US Dividend Aristocrats ETF	Yes	Return Orie	Dividend Screened/Weighted	0.3500	S&P High Yield Dividend Aristcrts
<input type="checkbox"/>	3 iShares European Property Yield	Yes	Return Orie	Dividend Screened/Weighted	0.4000	FTSE EPRA/NAREIT Dv Eur Ex UK
<input type="checkbox"/>	4 iShares UK Dividend	Yes	Return Orie	Dividend Screened/Weighted	0.4000	FTSE UK Dividend Plus NR GBP
<input type="checkbox"/>	5 iShares STOXX Global Sel Div 100 (DE)	Yes	Return Orie	Dividend Screened/Weighted	0.4600	STOXX Global Select Dividend 10
<input type="checkbox"/>	6 Lyxor ETF JPX-Nikkei 400 Daily Hdg C-GBP	Yes	Return Orie	Quality	0.2500	JPX Nikkei 400 NR JPY

### Asset Flows

Market Summary	Workspace	Custom Report	Search	Advanced Search			Help
Market	Europe ETFs (domiciled)	Market Note	Eff. Date: 2015-04-30	Currency: EUR	Snapshot: 7-May 21:03 CDT		
Mkt Sh Basis	Total Net Assets						

### ▼ Strategic Beta/Other Funds

Name	Estimated Net Flow (€Mil)				Market Share Basis: Total Net Assets (€Bil)					
	1-Mo	QTD	YTD	1-Yr	04-2015	Mkt Sh%	Rank	04-2014	Mkt Sh%	Rank
Strategic Beta, Return-Oriented	185	185	3,181	5,291	22	4.89	2	13	4.16	2
Strategic Beta, Risk-Oriented	84	84	781	1,931	4	0.81	3	1	0.46	4
Strategic Beta, Other	30	30	225	557	3	0.67	4	3	0.80	3
Other Funds	3,248	3,248	30,506	56,004	428	93.62	1	301	94.58	1

Drill-down View Chart

## A Global Guide to Strategic-Beta Exchange-Traded Products

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### Executive Summary

- ▶ “Smart beta” is an unfortunate name, one that has positive connotations that may not always be warranted.
- ▶ What Morningstar deems “strategic beta” is a broad and rapidly growing category of benchmarks and the investment products that track it.
- ▶ As of June 30, 2014, there were 673 strategic-beta exchange-traded products, or ETPs, with collective assets under management of approximately \$396 billion worldwide.<sup>1</sup>
- ▶ Strategic-beta ETPs are making inroads against their peers that are benchmarked to more-traditional indexes. While their market share has been increasing in every region we have examined, they have made greater inroads in large, more mature markets than they have in smaller, less developed ones. For example, strategic-beta ETPs accounted for 19% of U.S. ETP assets, but just 1.5% of ETP assets in the Asia-Pacific region.
- ▶ The common thread among strategic beta investment products is that they seek to either improve their return profile or alter their risk profile relative to more-traditional market benchmarks.
- ▶ As new products have continued to roll off asset managers’ assembly lines, their sales and marketing departments have been working tirelessly to position these new models in an increasingly competitive field.
- ▶ The result has been a ratcheting up of the level of complexity of the indexes that underlie these benchmark-based investment products and, in some cases, a growing disparity between how they are pitched by their sponsors and the actual investment results they produce.
- ▶ The need to define, measure, and police this space has grown and will continue to grow with time.
- ▶ At Morningstar, we are positioning ourselves to meet these needs, with the goal of helping investors make better-informed investment decisions.
- ▶ This report is split into three “acts.” In the first act, we examine the global strategic-beta ETP landscape, looking at trends in asset growth, asset flows, product development, and focus on a region-by-region basis. In the second act, we discuss the “origins” of strategic beta, looking at the various types of risk that these strategies look to harness and how they manifest themselves in an investment context. Finally, in the third act, we provide a practical guide to analyzing strategic-beta ETPs through a number of different lenses that will help investors make more-informed decisions when considering these products.

<sup>1</sup> All monetary figures throughout this report are expressed in U.S. dollars unless otherwise stated.

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