

STOXX Ltd. response to Consultation Paper

of the
European Banking Authority

On appropriately diversified indices under Article 344(1) of the
draft Capital Requirements Regulation (CRR)

Zurich, 6 September 2013

Introduction

STOXX is pleased to have the opportunity to submit comments to the European Banking Authority in response to their “Consultation Paper – On appropriately diversified indices under Article 344(1) of the draft Capital Requirements Regulation (CRR).

The Consultation Paper proposes these draft Implementing Technical Standards (ITS) in accordance with Article 344(1) of the draft Capital Requirements Regulation (CRR) relating to the identification of relevant appropriately diversified indices for the purposes of calculating the capital requirements for equity risk according to the standardized rules. This is necessary as the CRR text considers that stock-index futures, which are both exchange traded and ‘appropriately diversified’, only pose general risk for an institution. Consequently, these ITS list the exchange traded and appropriately diversified indices, for which specific risk can be ignored.

To ensure that the specific risk incorporated in a stock index can be dismissed, the minimum level of diversification required in these draft ITS takes into account a number of considerations: in particular, (i) the index must comprise a minimum number of equities; (ii) none of the equities (or concentration of equities) must significantly influence the volatility of the index and hence not represent more than a certain percentage of the total index value; finally, the index must comprise of equities diversified both (iii) from a geographical and (iv) an economical perspective.

STOXX Limited is an established index specialist with a European heritage. The launch of the first STOXX[®] indices in 1998, including the EURO STOXX 50[®] index, marked the beginning of the STOXX business activities. Since that time, STOXX has been continuously expanding its portfolio of indices, and now operates on a global level, across all asset classes. STOXX Limited is committed to delivering its high-quality, reliable and trusted index offerings to its global client base.

Our indices are licensed to the world's largest issuers of financial products, capital owners and asset managers, in total to more than 400 companies around the world, and are used not only as underlying for financial products such as exchange-traded funds (ETFs), futures and options, and structured products, but also for risk and performance measurement.

We would welcome the opportunity to discuss the content of our submission with you further.

Should you require any additional information in the meantime, please contact: Dr. Hartmut Graf, CEO, STOXX Ltd., Selnaustrasse 30, 8021 Zurich, Switzerland, Hartmut.Graf@stox.com.

We are happy for our comments to be made public.

A. Proposed regulation

According to the draft regulation proposed to the European Parliament and the Council in relation to Article 344 (4) of the CRR Regulation: "... the specific risk can be ignored for stock-index futures which are exchange traded and represent a relevant appropriately diversified index. Therefore, the exchange traded indices listed in this Regulation should be considered as appropriately diversified where it can be assumed that they represent no specific risk. This, in turn, should be the case where the indices meet all of the following criteria: they contain at least 20 equities; in terms of concentration, no single entity contained within them represents more than 25% of the total index, while 10% of the largest equities (rounding up the number of equities to the superior natural number) represent less than 60% of the total index; in terms of diversification they encompass equities from at least a national market, and they comprise equities from at least four industries amongst oil and gas, basic materials, industrials, consumer goods, health care, consumer services, telecommunications, utilities, financials and technology."

B. Interpretation

The EBA has determined its view on how to fulfill the aforementioned requirements on diversification based on the following set of criteria:

- 1. Number:** a diversified index shall contain at least 20 equities.
- 2. Concentration:** a) by equity: No single equity shall represent more than 25% of the total index; b) by group of equities: 10% of the largest equities (rounding up to the superior natural number) shall represent less than 60% of the total index.
- 3. Diversification by Geography:** it shall encompass equities from at least one national market; no regional indices shall be recognized as appropriately diversified.
- 4. Diversification by Industry:** the index shall comprise equities from at least 4 industries amongst the following ones: Oil & Gas, Basic Materials, Industrials, Consumer Goods, Health care, Consumer Services, Telecommunications, Utilities, Financials, Technology.

C. Comments

1. For every index provider there are some sector indices that do contain less than 20 equities. Instead of focusing on a number of equities it would make more sense to focus on distribution and weightings within an index. This would also be in line with requirements from ESMA / UCITS regulation and would therefore for greater consistency and harmonization within the regulation.
2. We do not assess the proposed concentration rules as appropriate. We rather suggest to adopt the already existing ones, which already have demonstrated to be efficient ESMA / UCITS rules with concentration criteria of 35% and 20%.
3. Regional indices are systematically better diversified than national indices. Taking this into account it is not clear why regional indices shall not be recognized as appropriately diversified. Also it remains unclear to us why an appropriately diversified index shall encompass at least one national market, while a multitude of encompassed national markets may lead to comprise a specific region.
4. We do not believe that diversification by industry is appropriate because this way sector specific indices are systematically being excluded although these indices may generally comply with UCITS industry diversification requirements in terms of concentration, weights and geographical diversification.

Furthermore, we would like to draw your attention also to the following comments:

- a) In case of implementation, the interpretation on "Concentration by group of equities: 10% of the largest equities" could be referred more precisely, e.g. by referring 10% to market capitalization (before / after capping), weighting in the index, or e.g. 10% of the number of shares.
- b) The industrial diversification refers to ICB data (based on FTSE). The industrial groups are in largely accepted used. The STOXX index universe does already adhere to these industry groups. However other indices as e.g. the DAX index universe may very well have a different industrial logic that does not correspond completely with the ICB data. It is seems useful to allow also other distinction logics.
- c) The annexed list is reviewed annually in September. The validity expires January 1 of the following year for an entire year, but there is no in-year review.
- d) On "Annex 1 - Stock indices meeting the requirements of Article 344" of the proposed Regulation the Euro STOXX 50 is listed under its old name DJ Euro STOXX 50. Kindly correct his to the current naming: Euro STOXX 50.

In relation to all these comments we may answer to your questions more concisely as follows:

Questions for Consultation

Q1. Do you agree with the set of criteria proposed for determining whether an index is diversified? Are there any other criteria that should be considered?

We do not agree with the set of criteria proposed. There is no index methodology that may cover all the criteria cumulatively in general. We think that the existing ESMA / UCITS criteria should be considered.

Q2. Do you believe that the levels and numbers of the proposed criteria are appropriate?

We do not think that the levels and numbers of the proposed criteria are appropriate. Instead we suggest adopting the existing UCITS levels of 35% and 20%.

Q3. Are there any relevant indices not listed in Annex I that meet the criteria? Please provide evidence that such indices meet the criteria defined in this draft ITS.

We attach a list of other indices not mentioned in Annex I of which we think that they meet the proposed criteria, or where applicable, in disagreement of the criteria requirements would still be considered as appropriately diversified or where there are already stock index futures outstanding.

Yours sincerely,
STOXX LIMITED

Attachment:

List of indices to be added to Annex I

RIC Code	Name	Comment
.STOXX50E	EURO STOXX 50	already listed
.STOXX50	STOXX Europe 50	to be added to list; fulfills all requirements; existing futures
.STOXX	STOXX Europe 600	to be added to list; fulfills all requirements; existing futures
.LCXP	STOXX Europe Large 200	to be added to list; fulfills all requirements; existing futures
.MCXP	STOXX Europe Mid 200	to be added to list; fulfills all requirements; existing futures
.SCXP	STOXX Europe Small 200	to be added to list; fulfills all requirements; existing futures
.SD3E	EURO STOXX Select Dividend 30	to be added to list; fulfills all requirements; existing futures
.STOXXE	EURO STOXX	to be added to list; fulfills all requirements; existing futures
.LCXE	EURO STOXX Large	to be added to list; fulfills all requirements; existing futures
.MCXE	EURO STOXX Mid	to be added to list; fulfills all requirements; existing futures
.SCXE	EURO STOXX Small	to be added to list; fulfills all requirements; existing futures
.SX5NFE	EURO STOXX 50 ex Financials	to be added to list; fulfills all requirements; existing futures
.SXP	STOXX Europe 600 Retail	We disagree with Industry requirement
.SXQP	STOXX Europe 600 Personal & Household Goods	We disagree with Industry requirement
.SX3P	STOXX Europe 600 Food & Beverage	We disagree with Industry requirement
.SX4P	STOXX Europe 600 Chemicals	We disagree with Industry requirement
.SX6P	STOXX Europe 600 Utilities	We disagree with Industry requirement
.SX7P	STOXX Europe 600 Banks	We disagree with Industry requirement
.SX8P	STOXX Europe 600 Technology	We disagree with Industry requirement
.SXAP	STOXX Europe 600 Automobiles & Parts	We disagree with Industry requirement
.SXDP	STOXX Europe 600 Health Care	We disagree with Industry requirement
.SXEP	STOXX Europe 600 Oil & Gas	We disagree with Industry requirement
.SXFP	STOXX Europe 600 Financial Services	We disagree with Industry requirement
.SXTP	STOXX Europe 600 Travel & Leisure	We disagree with Industry requirement
.SXIP	STOXX Europe 600 Insurance	We disagree with Industry requirement
.SXKP	STOXX Europe 600 Telecommunications	We disagree with Industry requirement
.SXMP	STOXX Europe 600 Media	We disagree with Industry requirement
.SXNP	STOXX Europe 600 Industrial Goods & Services	We disagree with Industry requirement
.SXOP	STOXX Europe 600 Construction & Materials	We disagree with Industry requirement
.SXPP	STOXX Europe 600 Basic Resources	We disagree with Industry requirement
.SX86P	STOXX Europe 600 Real Estate	We disagree with Industry requirement