

Indexing 360°: MSCI EMU vs EURO STOXX 50

UBS ETF **Market Matters**



Investors often choose between broad market and blue chip indices for core portfolios. For Eurozone equities, popular benchmarks include the broad MSCI EMU and blue-chip EURO STOXX 50.

The MSCI EMU index has on average outperformed the EURO STOXX 50 by 80 bps annually since 1999. MSCI EMU includes mid-cap stocks which are increasingly relevant and may provide excess returns associated with the size factor.

Index construction methodologies have implications for country and sector allocations which may affect performance.

MSCI country indices fare well in comparison to blue-chip stocks for most European markets.

Passive investing has developed as a convenient, liquid, and cost-efficient way to invest in flagship indices covering broad markets (e.g., S&P500) and blue chip stocks (e.g., Dow Jones 30). They constitute the core of passive portfolios and provide investors with the equity risk premium for bearing (undiversifiable) market risk. Investors have ample access to these exposures via ETFs, index funds, mandates, and other passive vehicles.

Broad market versus blue chips

Investors may consider differentiating features when deciding on the right benchmark. In the case of Eurozone equities, a popular choice is either the MSCI EMU or the EURO STOXX 50. MSCI EMU is a broad market index that selects companies which account for about 85% of the total market capitalization on a free-float adjusted basis. In contrast, the EURO STOXX 50 is a bluechip index that includes the 50 largest companies in the Eurozone (also free-float adjusted).

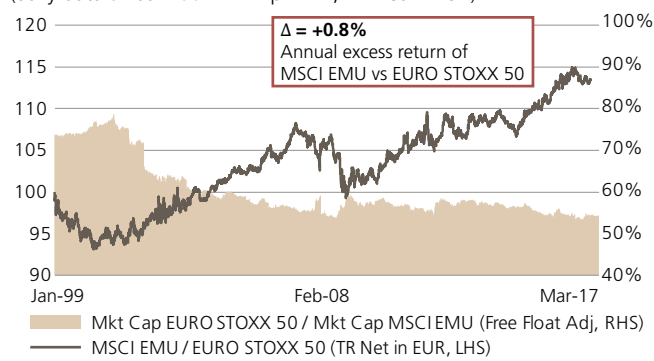
The MSCI EMU includes mid-cap stocks and has on average outperformed the EURO STOXX 50 by 80 bps per annum since Jan '99 (Figure 1). It is consistent with the premise that smaller companies tend to provide higher returns (i.e., the size factor premium). Indeed, the smallest company in MSCI EMU is worth EUR 2.7, while in EURO STOXX 50 it stands at EUR 15.9 bn (as of April 2017).

Market coverage

The MSCI EMU Index maintains a coverage of 85% of the total market capitalization and thus has provided good market representation and diversification through the years. In contrast, the EURO STOXX 50 market coverage has declined: in 1999 it represented 73% of MSCI EMU, but that has now decreased to 54% in 2017 (Figure 1).

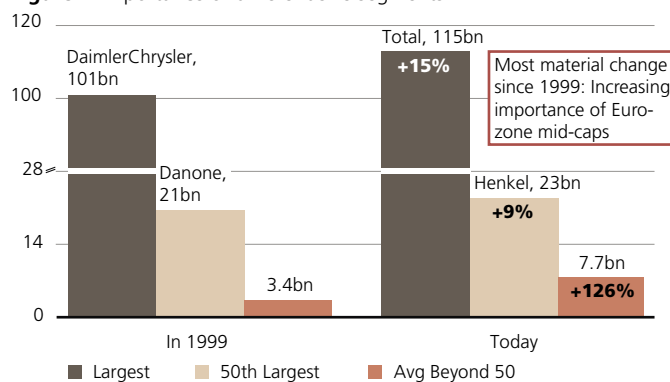
The EURO STOXX 50 has become less representative due to the growing relevance of mid-cap stocks. For example, in 1999 a company outside the top 50 rank by market cap in the MSCI EMU was worth on average EUR 3.4bn, but that has increased by as much as 126% to EUR 7.7bn by 2017 (Figure 2). Over the same period, the single largest company saw its market capitalization grow by a modest 14%, while the 50th largest company by only 9%. Moreover, it's reasonable to expect the relevance of the top 50 stocks to decrease over time as this fixed number will be an increasingly smaller fraction of the total number of listed companies.

Figure 1: Relative performance of MSCI EMU vs Euro Stoxx 50 (daily data 31 Jan '99 – 14 April '17, TR Net in EUR)



Source: Bloomberg, UBS Asset Management, data as of 13 April, 2017.

Figure 2: Importance of different size segments



Source: UBS Asset Management, data as of 28 February 2017.



Index construction methodologies

MSCI EMU

MSCI standard indices aim to cover 85% of the investible market capitalization on a free-float adjusted basis¹. MSCI EMU is constructed using a bottom up approach which sums up MSCI indices for individual Eurozone countries, each of which also covers 85% of a single country market. This ensures that MSCI EMU exhibits good country diversification. The indices are rebalanced quarterly and semi-annually to ensure timely updates reflecting market changes.

EURO STOXX 50

EURO STOXX 50 selects the 50 largest companies in the Eurozone subject to certain industry constraints. Specifically, a selection list of companies is first created to include stocks covering 60% of the free-float adjusted market capitalization within each of 19 EURO STOXX Supersector indices. Subsequently, 40 of the largest stocks are selected from this universe and additional top 10 stocks are taken from a buffer group of existing index constituents ranked between 41 and 60 by market capitalization.² The minimum liquidity requirements of the parent EURO STOXX index are applied. The index is fully reviewed annually, while the components are capped at 10% every quarter.

¹ For further details on index methodology see "MSCI Global Investable Market Indexes Methodology Summary", May 2014 or the official index methodology document. For example, MSCI considers a company to be investible if it meets the minimum market caps, free-float and liquidity requirements.

² For detail on index methodology see "STOXX® Index Methodology Guide (Portfolio Based Indices)", March 2017.

Sector and country allocations

MSCI EMU and EURO STOXX 50 have different country allocations. For example, MSCI EMU has an underweight of about 4% to Germany and France relative to the EURO STOXX 50 (Figure 3). That is likely because these two countries have the biggest domestic markets and thus some of the largest companies. The MSCI EMU methodology (i.e., bottom up country-by-country aggregation) ensures that country allocation are in close proportion to the respective stock market caps, while EURO STOXX 50 selects companies irrespective of domicile countries.

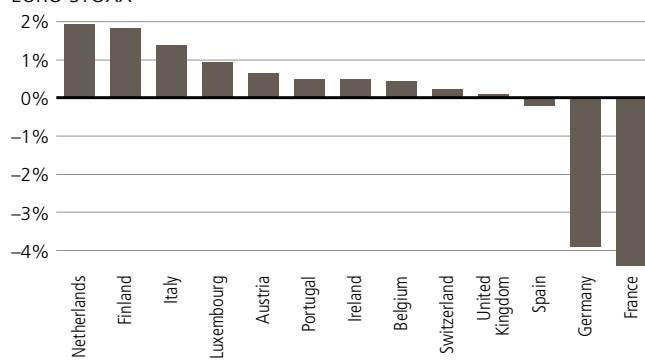
Similarly, the index construction methodologies have implications for sector allocations with MSCI EMU having for example a 2.5% overweight in Consumer Discretionary and about a 2% underweight in Materials and Financials (Figure 4). MSCI EMU is sector agnostic, while EURO STOXX 50 has industry constraints such that it can include no more than 60% of the free-float market capitalization of any of the EURO STOXX Supersector indices.

Country indices

Another relevant question is whether to choose broad market or blue chip indices for individual countries. Comparing annualized return differentials across five major European markets reveals that broad market MSCI indices in most cases outperformed regional blue-chips (data from Jan '99 to March '17). The largest differential is for Switzerland of 20 bps per annum, followed by Spain with 18 bps (Figure 5).

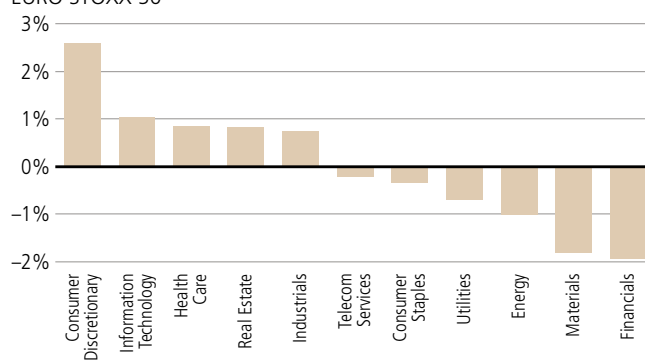
The country blue-chip indices select a different number of stocks: the Swiss SMI index picks the largest 20, Spanish Ibex takes 35, German DAX chooses 30, British FTSE picks 100, and French CAC40 selects top 40. It is clear that the EURO STOXX 50 has a much higher threshold in terms of size than these regional blue chip indices, but they still have a bias towards large stocks relative to corresponding MSCI country indices. Hence the size factor is also relevant, although its impact is considerably smaller than in the case of MSCI EMU vs. EURO STOXX.

Figure 3: MSCI EMU country overweights and underweights vs EURO STOXX



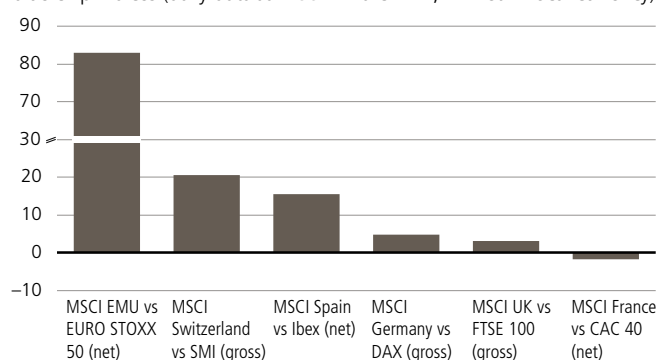
Source: Bloomberg, UBS Asset Management, data as of 26 April 2017.

Figure 4: MSCI EMU sector overweights and underweights vs EURO STOXX 50



Source: Bloomberg, UBS Asset Management, data as of 26 April 2017.

Figure 5: Average annualized differential between MSCI indices and blue chip indices (daily data Jan '99 – March '17, TR Net in local currency)



Source: Bloomberg, UBS Asset Management, data as of 31st March, 2017.

Past performance is not indicative of possible future returns.

Pawel Janus

PhD, Head Passive Research, Director
UBS Asset Management

Marcin Wojtowicz

PhD, Passive Research, Associate Director
UBS Asset Management

For more information, visit our homepage. www.ubs.com/etf



Bloomberg: UETF <GO>

E-Mail: ubs-etf-uk@ubs.com

Website: www.ubs.com/etf

Andrew Walsh

Head UBS ETF UK & Ireland
Tel. +44-20-7901-5901
Mob. +44-78-1804-7240
andrew.walsh@ubs.com

Florian Cisana

UBS ETF UK & Ireland
Tel. +44-20-7901-5398
Mob. +44-78-8009-6848
florian.cisana@ubs.com

Expand your portfolio with UBS ETFs.

Fund Name	Fee	AuM (GBPm)	NAV ccy	Replication	Distribution	ISIN	Bloomberg
UBS ETF (LU) EURO STOXX 50 UCITS ETF	0.15%	565	EUR	Physical	Yes	LU0136234068	UB01 LN
UBS ETF (LU) MSCI EMU UCITS ETF	0.18%	2'541	EUR	Physical	Yes	LU0147308422	UB06 LN
UBS ETF (LU) MSCI EMU UCITS ETF	0.18%		EUR	Physical	No	LU0950668870	EMUAA SW
UBS ETF (LU) MSCI EMU hedged CHF UCITS ETF	0.28%	374	CHF	Physical	No	LU0950669175	EUCHBH SW
UBS ETF (LU) MSCI EMU hedged GBP UCITS ETF	0.28%	81	GBP	Physical	Yes	LU0937835733	UC59 LN
UBS ETF (LU) MSCI EMU hedged GBP UCITS ETF	0.28%		GBP	Physical	No	LU0950669688	UC60 LN
UBS ETF (LU) MSCI EMU hedged USD UCITS ETF	0.28%	827	USD	Physical	Yes	LU0937835576	UC89 LN
UBS ETF (LU) MSCI EMU hedged USD UCITS ETF	0.28%		USD	Physical	No	LU0950669415	EUUSBH SW
UBS ETF (LU) FTSE 100 UCITS ETF	0.20%	108	GBP	Physical	Yes	LU0136242590	UB03 LN
UBS ETF (IE) FTSE 100 SF UCITS ETF	0.22%	12	GBP	Synthetic	No	IE00B3X0KQ36	F1GBAS SW
UBS ETF (LU) MSCI United Kingdom UCITS ETF	0.20%	710	GBP	Physical	Yes	LU0937836467	UC63 LN
UBS ETF (LU) MSCI United Kingdom UCITS ETF	0.20%		GBP	Physical	No	LU0950670850	UC64 LN
UBS ETF (LU) MSCI United Kingdom hedged CHF UCITS ETF	0.30%	527	CHF	Physical	No	LU0950671072	UKCHBH SW
UBS ETF (LU) MSCI United Kingdom hedged EUR UCITS ETF	0.30%	365	EUR	Physical	Yes	LU0937836970	UKEUAH SW
UBS ETF (LU) MSCI United Kingdom hedged EUR UCITS ETF	0.30%		EUR	Physical	No	LU0950671239	UKEUBH SW
UBS ETF (LU) MSCI United Kingdom hedged USD UCITS ETF	0.30%	564	USD	Physical	Yes	LU0937837275	UKUSAH SW
UBS ETF (LU) MSCI United Kingdom hedged USD UCITS ETF	0.30%		USD	Physical	No	LU0950671403	UKUSBH SW
UBS ETF (LU) MSCI Switzerland UCITS ETF	0.20%	582	CHF	Physical	Yes	LU0979892907	SW2CHA SW
UBS ETF (LU) MSCI Switzerland UCITS ETF	0.20%		CHF	Physical	No	LU0977261329	SW2CHB SW
UBS ETF (LU) MSCI Switzerland hedged GBP UCITS ETF	0.30%		GBP	Physical	Yes	LU1169830442	UC94 LN
UBS ETF (LU) MSCI Switzerland hedged GBP UCITS ETF	0.30%		GBP	Physical	No	LU1169830525	UC93 LN
UBS ETF (LU) MSCI Switzerland hedged EUR UCITS ETF	0.30%	164	EUR	Physical	Yes	LU0979892220	S2EUAH SW
UBS ETF (LU) MSCI Switzerland hedged EUR UCITS ETF	0.30%		EUR	Physical	No	LU0977260941	S2EUBH SW
UBS ETF (LU) MSCI Switzerland hedged USD UCITS ETF	0.30%	117	USD	Physical	Yes	LU0979892659	S2USAH SW
UBS ETF (LU) MSCI Switzerland hedged USD UCITS ETF	0.30%		USD	Physical	No	LU0977261089	S2USBH SW

Source: UBS Asset Management, data as of 28 April 2017

Find all product details here:

[› UBS ETF Product Overview](#)

For marketing and information purposes by UBS

UBS Global Asset Management (UK) Ltd is a subsidiary of UBS AG. Registered in England. UBS Global Asset Management (UK) Ltd and UBS Global Asset Management Funds UBS Asset Management (UK) Ltd is a subsidiary of UBS AG. Registered in England. UBS Asset Management (UK) Ltd and UBS Asset Management Funds Ltd are authorised and regulated by the Financial Conduct Authority. UBS Asset Management Life Ltd is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority. Telephone calls may be recorded.

This document is for Professional Clients only. It is not to be distributed to or relied upon by Retail Clients under any circumstances.

The document has not been prepared in line with the FCA requirements designed to promote the independence of investment research and is not subject to any prohibition on dealing ahead of the dissemination of investment research.

The Luxembourg and Irish domiciled funds are recognised scheme under section 264 of the Financial Services and Markets Act 2000. They seek UK Reporting Fund Status.

The protections offered by the UK's regulatory system, and compensation under the Financial Services Compensation Scheme, will not be available.

The Switzerland domiciled funds are not recognised under section 264 of the Financial Services and Markets Act and are therefore subject to the restrictions on promotion in section 238 of the Financial Services and Markets Act.

The returns payable to the fund are dependent on payments received by the fund from the swap counterparty under the terms of the relevant swap and, therefore are subject to credit risk of the swap counterparty. In the event that the swap counterparty defaults under the terms of the relevant swap, the funds may suffer a loss.

This material supports the presentation(s) given. It is not intended to be read in isolation and may not provide a full explanation of all the topics that were presented and discussed. Care has been taken to ensure the accuracy of the content, but no responsibility is accepted for any errors or omissions. Please note that past performance is not a guide to the future. The value of investments and the income from them may go down as well as up, and investors may not get back the original amount invested. This document is a marketing communication. Any market or investment views expressed are not intended to be investment research.

The document has not been prepared in line with the FCA requirements designed to promote the independence of investment research and is not subject to any prohibition on dealing ahead of the dissemination of investment research. The information contained in this document should not be considered a recommendation to purchase or sell any particular security and the opinions expressed are those of UBS Asset Management and are subject to change without notice. Furthermore, there can be no assurance that any trends described in this document will continue or that forecasts will occur because economic and market conditions change frequently. This document does not create any legal or contractual obligation with UBS Asset Management. The recipient agrees that this information shall remain strictly confidential where it relates to the Investment Manager's business. The prior consent of UBS Asset Management (UK) Ltd should be obtained prior to the disclosure of commercially sensitive information to a third party (excluding the professional advisors of the recipient). Information reasonably deemed to be commercially sensitive and obtained from UBS Asset Management (UK) Ltd should not be disclosed. This information is supplied with a reasonable expectation that it will not be made public. If you receive a request under the Freedom of Information Act 2000 for information obtained from UBS Asset Management (UK) Ltd we ask that you consult with us. We also request that any information obtained from UBS Asset Management (UK) Ltd in your possession is destroyed as soon as it is no longer required. This document may not be reproduced, redistributed or republished for any purpose without the written permission of UBS AG.

This document is issued by [UBS Asset Management (UK) Ltd] and is intended for limited distribution to the clients and associates of UBS Asset Management. Use or distribution by any other person is prohibited. Copying any part of this publication without the written permission of UBS Asset Management is prohibited. Care has been taken to ensure the accuracy of its content, but no responsibility is accepted for any errors or omissions herein.

© UBS 2017. The key symbol and UBS are among the registered and unregistered trademarks of UBS. All rights reserved.

