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Asian institutions to increase allocations for ETPs, signaling tremendous growth opportunities, State Street Global Advisors survey shows

Singapore, Oct 18, 2012 —Institutions are expected to increase allocations for exchange-traded products (ETPs) in the Asia Pacific region, signalling tremendous growth opportunities, according to a survey commissioned by State Street Global Advisors (SSgA) and conducted by Greenwich Associates.

The study of institutional investors across the region, conducted in July and August of this year, aims to assess the extent to which institutions use ETPs and to gain a better understanding the role of ETPs for these institutions within their portfolios.

In the Asia Pacific region, institutional allocations are estimated to comprise of the majority of the ETP assets under management in the region, according to the study. About 80 percent of Asian institutions and distributors who participated in the study currently allocate up to 5 percent of their assets to ETPs. While this percentage represents a small proportion of their overall portfolios, this breakdown is similar to trends in other markets where institutional allocations are only a small percentage of their total investible pie. The total value of assets under management among Asia Pacific domiciled ETPs stands at roughly US$118 billion, according to Bloomberg data.

Mr Frank Henze, Head of Exchange Traded Funds, Asia Pacific, at State Street Global Advisors said, “Institutions in AsiaPacific are now managing more money than they did previously. That growth is going to fuel the demand for more diverse investments. Although current ETP allocations are small relative to institutions’ total assets under management across all regions, indications that institutional investors will increase their ETP allocations in the coming years, signals tremendous growth opportunities, not only in Asia but also globally.”

More than 40 percent of the asset managers and distributors who participated in the study said they expect to increase their use of ETPs in coming years, with an additional 46 percent stating that they will continue their current allocations to ETPs.

Approximately 50 percent of study respondents employ ETPs in equities covering Asian/emerging markets, domestic exposure, international and other regional equities. The use of ETPs for exposure to commodity is also frequently mentioned. Meanwhile, only about one-quarter or less of Asian institutions invest in ETPs for fixed income.

The study results also show that many Asian institutions view ETPs as one of the main ways to access desired exposures. As awareness improves, institutions are hearing the message that ETPs have more benefits, such as cost efficiency, transparency, diversification and built-in liquidity. As education of both the institutional and retail markets increase, the use of ETPs is expected to pick up greater momentum.

Asian institutions expect to expand their use of these products mainly in equities, particularly those that provide exposure to international, domestic, Asian and emerging markets and access to specific markets that would otherwise be difficult or expensive to access through mutual funds or other products.

Mr Henze noted, “Currently institutional investors in Asia most commonly use ETPs for strategic applications such as obtaining investment exposures required in executing portfolio strategies and as a tool for hedging and risk management. These strategic uses may represent longer-term allocations to the market, leading to stickier assets compared to allocations used for more tactical purposes. Fewer institutions in Asia use ETPs in tactical investment functions, such as cash equitisation, rebalancing, and manager transitions so we believe this area represents a strong growth opportunity for increased ETP uptake in the region, in both volatile and more steady market environments.

According to the study, the three most common applications of ETPs among institutions in Asia are: 1) obtaining beta exposures when implementing core/satellite portfolio constructions, 2) portfolio completion and 3) hedging/risk management. Other applications such as cash equitisation, while common in the United States, are less common to Asian investors. This demonstrates that further use in a large variety of applications represent new growth drives for ETPs in Asia.

“Cash equitisation is one clear example of how the lessons learned by institutions in other markets may benefit Asian investors and accelerate the proliferation of ETPs in institutional portfolios here,” says Abhi Shroff, Greenwich Associates consultant. “At a time when cash holdings are yielding historically low rates of return, it is in the interest of Asian institutions to investigate the benefits of this tactical play.”

Although some institutions say they would like to see more liquid Asian and domestic equity ETPs, the driver of institutional demand for ETPs in the near term is not likely to be the launch of new products, but rather improved sell-side support for existing offerings.

In conclusion, the study said that institutions in Asia are still mobilizing to take advantage of the full range of benefits that ETPs provide. Asian institutions use ETPs most often in core/satellite portfolios. Experiences of developed-market institutions reveal an array of additional tactical and strategic applications that are as yet underexplored by most institutions in Asia. As the Asian investable institutional asset pool is expected to continue its upward climb, ETPs are well positioned to capture strong allocations in the region. Additionally, in conjunction, with some of the world's biggest ETP providers stepping up the quality and intensity of their educational efforts and client service, demand for ETPs among Asian institutions could increase dramatically in coming years.

For the study, Greenwich Associates interviewed 58 asset managers and proprietary traders in Japan and 65 institutional investors and distributors in Asia (ex-Japan), including 13 in China, 12 in Hong Kong, 12 in Taiwan, 10 in South Korea and nine each in Singapore and Australia.

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[1] As at 30 September 2012.

[2] As of September 30, 2012. This AUM includes the assets of the SPDR Gold Trust (approx. $75.4 billion as of September 30, 2012) for which State Street Global Markets, LLC, an affiliate of State Street Global Advisors, serves as the marketing agent.

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