



## FTSEUROFIRST INDICES & DERIVATIVES

# ALTERNATIVE INDICES ARRIVE AT LONG LAST

Demand has been high for indices that reflect recent currency changes in the trading marketplace and the broader European landscape

Today's market conditions and Europe's expanding horizons require new index products. The main European index, for example, is now over five years old – predating both the euro and the end of the 1990s bull market. At the beginning of the year, the demanding brief given to FTSE and Euronext by institutional investors seeking alternative solutions to those currently available was as follows:

- Develop a new tradable index series for Europe
- Ensure the indices are more representative of the eurozone and pan-European landscapes
- Keep tracking error (relative to broader benchmarks) as low as possible without losing the tradability of the index series
- Provide market participants with an alternative tradable product to the existing series of narrow based indices.

## » SERIES LAUNCHED

The result of this demand, the FTSEurofirst tradable index series, was launched jointly by Euronext, the world's first cross-border exchange for cash and derivatives products, and FTSE, the global index provider, in April of this year. The index series covers the eurozone with the FTSEurofirst 80 index and pan-Europe (eurozone and UK) with the FTSEurofirst 100 index.

The FTSEurofirst 80 comprises 80 of the most liquid constituents in eurozone countries, whilst the FTSEurofirst 100 index comprises 100 of the most liquid eurozone and UK constituents. Both indices have been welcomed as a long overdue alternative to the crop of tradable but narrow based indices and the broader but less liquid indices.

The two were designed to provide an alternative to the current range of indices that were deemed by market practitioners to be too narrow to accurately reflect eurozone or pan-European performance. Moreover, institutional investors with funds benchmarked to the broader range of indices, like the FTSE Eurobloc index, typically had only one liquid derivative contract available for hedging exposure or efficient portfolio management purposes. This is no longer the case. Euronext.liffe – the derivatives business of Euronext – launched FTSEurofirst index futures and options on 23 June of this year.



**'With the arrival of the euro in 1999, there has been a gradual demand for indices and products that expose investors to the performance of the eurozone'**

Ade Cordell, Euronext.liffe

The new indices combine broader constituent coverage, better eurozone and UK representation and better tracking error than other pan-European tradable indices. Tracking error is the margin from which a portfolio or fund deviates from a given strategy or benchmark index. It is the low tracking error figures displayed by both indices that often attracts the most attention from fund managers. (See Chart 1.)

With the arrival of the euro in 1999, there has been a gradual demand for indices and products that expose

### FIVE YEAR TRACKING ERROR COMPARISON

1

	FTSE Eurobloc	MSCI EMU
FTSEurofirst 80	2.07%	2.20%
DJ Euro STOXX <sup>SM</sup> 50	3.73%	3.26%
	FTSE Europe	MSCI Europe
FTSEurofirst 100	2.68%	2.72%
DJ STOXX <sup>SM</sup> 50	4.09%	3.50%

Source: FTSE

**CONSTITUENTS & THEIR PERCENTAGE WEIGHTINGS REPRESENTED IN THE FTSEUROFIRST 100 AND 80 INDICES**

**2**

Index	FTSEUROFIRST 100 INDEX		FTSEUROFIRST 80 INDEX	
	No. of cons	% Wgt of domestic Indices	No. of cons	% Wgt of domestic indices
AEX	10	77.3%	12	84.1%
CAC 40	22	77.9%	27	88.1%
DAX 30	11	68.9%	17	86.4%
FTSE 100	41	80.9%	0	0.0%
HEX 25	3	58.7%	3	58.7%
IBEX 35	8	62.0%	10	67.2%
MIB 30	5	45.2%	11	68.9%

Source: FTSE

investors to the performance of the eurozone.

Interestingly, this has not led to a decline in the use of derivative products referenced to the domestic indices like the AEX in the Netherlands, the CAC 40 in France and the DAX 30 in Germany. Instead, there is constant demand for derivatives, warrants and funds referenced to both domestic and pan-European indices.

The FTSEurofirst index series should ensure that this trend continues the movement to make institutional style solutions open to private investors. Individual investors seeking to invest across the eurozone are unlikely to purchase individual funds referenced to all the local domestic indices. But investing in an exchange-traded

fund or “tracker” referenced to the FTSEurofirst 80 index, for instance, would give a private investor exposure to the well known domestic and international companies across eurozone through a single transaction.

**» DOMESTIC**

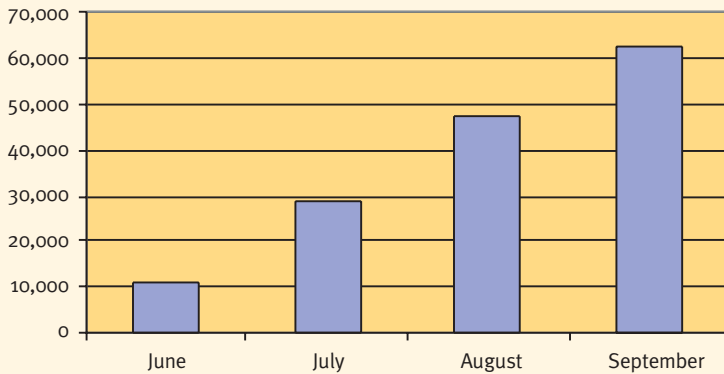
Chart 2 highlights both the number of constituents and their percentage weightings in the European domestic indices that are represented in the FTSEurofirst 100 and 80 indices. The table further illustrates that if we believe that the constituents of the local domestic indices are

**‘There is constant demand for derivatives, warrants and funds referenced to both domestic and pan-European indices’**



3

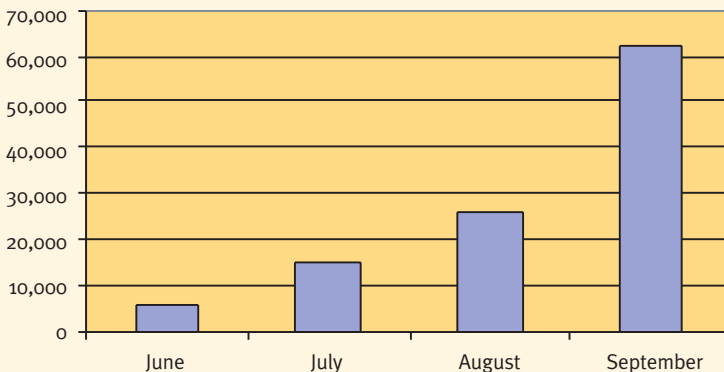
FTSEurofirst 80 derivatives volume



Source: Euronext.liffe

4

FTSEurofirst 100 derivatives volume



Source: Euronext.liffe

liquid and tradable then it is safe to assume that the FTSEurofirst indices, which are wholly comprised of constituents present in the main domestic indices, are by implication tradable indices themselves.

## RECENT ISSUANCE

Lyxor Asset Management recently listed a tracker referenced to the FTSEurofirst 80 index on the Euronext exchange in Paris. This tradable product gives private investors access to the performance of the FTSEurofirst 80 index.

Moreover, three warrants, a product which has so far proved to be more popular in continental Europe than in

analysis of back history data and synthetic futures prices before deciding to transact their first contract.

As the FTSEurofirst series were developed in response to the wishes of market participants the volumes captured in the contracts are evidently more than would be expected at this stage of a new product's life. The active participation of global product issuers like Société Générale and BNP Paribas are a good indication that the contracts meet the remit set by institutional investors at the outset.

With more product issuance envisaged over the coming months, the derivatives contracts are on course to gaining significant volume over the next 12 to 18 months.

*Ade Cordell, equity product management, Euronext.liffe*

the UK, have been launched by Société Générale referenced to the FTSEurofirst 80 index and a total of 10 further warrants were issued by BNP Paribas, five of which are referenced to the FTSEurofirst 80 and five to the FTSEurofirst 100.

## VOLUMES

The futures and options contracts were launched on 23 June this year. Since launch the contracts have traded more than 300,000 lots.

Volumes in the contracts are relatively low if compared to more mature index futures and options.

However, given that the contracts are a little over three months old and that the first series of products referenced to the contracts were available in mid to late September, the volume figures reached already are particularly impressive and the upward trend is encouraging. (See Charts 3 and 4.)

Exchange-traded derivative contracts typically build volume and open interest slowly. Market participants conduct detailed

## CORPORATE STATEMENT

Euronext.liffe is the derivatives business of Euronext, formed after Euronext's purchase of the London International Financial Futures and Options Exchange at the end of 2001. Euronext.liffe is the world's largest exchange, trading more business by value than any other exchange.



**Contact:**

- Kathryn Jaggard, Euronext.liffe, Cannon Bridge House, 1 Cousin Lane, London EC4R 3XX  
Tel: +44 (0)20 7379 2404  
Email: kathryn.jaggard@liffe.com