The nature and role of

financial benchmarks

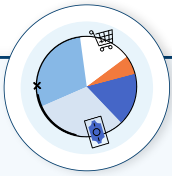
in supporting vibrant capital markets

What is a financial index?

Financial indexes or benchmarks measure the performance of financial instruments (e.g. stocks or bonds) , geographical markets, and sectors based on a methodology. As the combined value of the financial instruments in the index moves up or down, the index reflects that movement, commonly represented by a line on a graph.

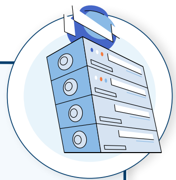
Indexes can, by themselves, not be invested in. However, indexes are used to create index-based products, such as Exchange-traded Funds (ETFs), thereby enabling passive and thematic investment. Index linked products help create liquidity, transparent and diversified investment opportunities for professional and retail investors at a competitive price.

Index providers are an important part of the financial value chain



Market data

Market makers and traders facilitate trading of financial instruments on the market (on or off exchange) **to determine the prices for financial instruments.**



Data providers and exchanges

Regulated data providers (e.g. stock exchanges) distribute raw data such as stock prices and financial statements, which are used as input by index providers **to create an index based on a pre-defined methodology.**

Index providers

Index providers act as service providers **developing an index methodology and administering the index.** They do so transparently and independently from any investment product that uses an index i.e. ETFs. Since 2016, index providers in the EU follow the EU Benchmark Regulation and are supervised.

Index users: asset managers, banks, and product issuers

Asset managers **create index-linked investment products,** such as Exchange-Traded Funds (ETFs), that mirror a specific index.

Investors

Professional or retail investors purchase, sell, and trade investment products e.g. ETFs.
Index providers administer the indexes; **asset managers manage the investment product based on the investors' choices.**

Indexes lower costs

Financial indexes are ***the* key enablers** of cost savings in capital markets.

Index-based investment products such as ETFs have saved investors €91 billion in European domiciled funds over the past 13 years. Moreover, the rise in index-based investment has led to a downward price pressure on the fees charged by active managers.

Index providers' role in the Capital Markets Union's value chain

Index providers are positioned at the centre of the value chain by measuring the performance of financial instruments, geographical markets, and sectors, based on a methodology.

Index providers purchase accurate and comprehensive financial market data (e.g. asset prices, trading volumes, and economic indicators) from data providers (e.g. stock exchanges) and use the data to develop and maintain indexes.

The core users of indexes (asset managers, custodians, banks, and asset owners) create investment products that mirror a specific index. Indexes cannot, by themselves, be invested in. However, indexes are used to create index-based products, such as ETFs, thereby enabling passive and thematic investment. Index products help create liquidity and reduce costs for all investors.

Index providers' function lies in-between data providers and index users. Index provider boil down data into understandable and useful information. Indexes allow their users to create investment products which offer transparent and diversified investment opportunities for professional and retail investors at a competitive price.

Developing the Capital Markets Union by enabling cost savings

The Capital Markets Union envisages many actions, but the ultimate aims are simple: to increase retail investor access and participation by facilitating diversified, cross-border investment opportunities at a low cost, in turn unlocking crucial capital for the European economy.

Index providers are key enablers of cost savings by increasing transparency for professional and retail investors, thus promoting the uptake of retail investment, and helping to develop a thriving Capital Markets Union.

Passive funds (e.g. ETFs) are, on average, cheaper than their active counterparts and provide investors with exposure to highly diversified, often thematically oriented portfolios (e.g. Technology), in a transparent and cost-efficient manner.[1] This affordability democratises access to financial markets, many of which were traditionally not accessible to retail investors, as well as promote cross-border investment within the European Union. The development of the Exchange-Traded Fund (ETF) market would not have been possible without index providers. Moreover, increasing fee pressures in the asset management industry and regulatory scrutiny of their fees have made index-based investing more attractive because of the inherent cost-savings.

The savings brought on by the index industry relative to its size and costs are of significant importance.

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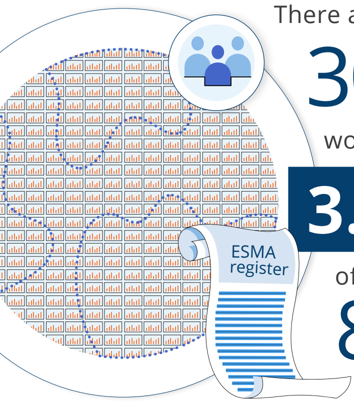
[1] EFAMA Factbook 2023

Facts about the index industry



There are approximately

300 index providers

worldwide administering around

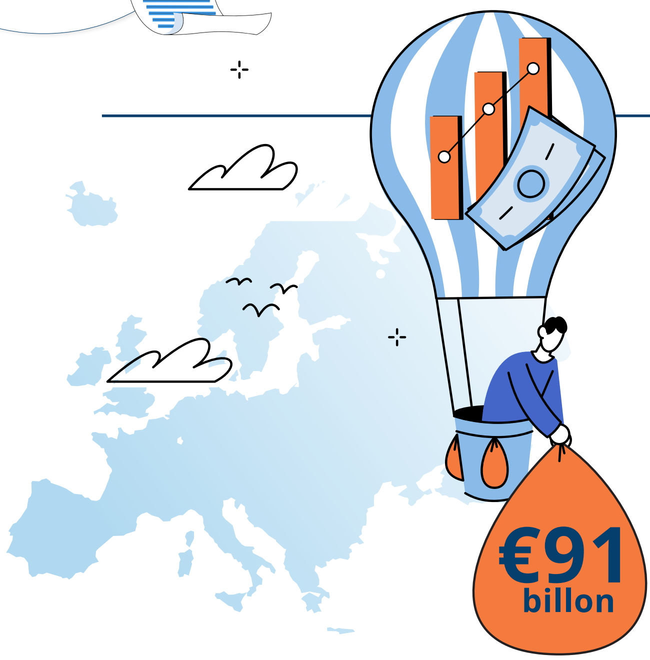
3.2 million indexes

of which

89 are in the ESMA register

Index providers' function lies in-between **data providers** and **index users**

allowing the data to be boiled down in to understandable and useful information, and index users such as asset managers to create investment products which offer transparent and diversified investment opportunities for professional retail investors at a competitive price.



Index-based investments, such as ETFs, has **saved** professional and retail investors **€91 billion** in European domiciled funds over the past 13 years.[2]

Moreover, the rise in index-investment has led to a downward price pressure on the fees charged by active managers

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[2] Vanguard calculations, using data from Morningstar, Inc.

About the IIA

Many of the leading independent index providers in the world are members of the IIA, including Bloomberg Indices, CBOE Global Indices, the Chicago Booth Center for Research in Security Prices (CRSP), China Bond Pricing Co. Ltd., China Securities Index Co. Ltd., FTSE Russell, Hang Seng Indexes, Morningstar, MSCI Inc., ICE, Korea Exchange, NASDAQ OMX, ParametaSolutions, Shenzhen Securities Information Co.Ltd.,S&P Dow Jones Indices LLC, ISS STOXX , and JPX Market Innovation and Research (Tokyo Stock Exchange). IIA members calculate over three million indices for their clients, covering a number of different asset classes, including equities, fixed income, and commodities. Part of the IIA's mission is to consider ways to promote best practices for index providers, which makes it a natural supporter of appropriate and proportionate industry standards. Our members are dedicated to promoting transparency, competition, sound operational practices, intellectual property rights, education, and effective index management practices. IIA members are independent index administrators who neither trade the underlying component securities of their indices nor directly create products for investors. Moreover, our members publicly make available methodologies, explain how their indices are created, calculated, or maintained. For more information http://www.indexindustry.org/

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