



## GLOBAL X INSIGHTS

# Covered Call & Growth: A Dividend Alternative with Equity Upside Potential

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*The derivative income ETF landscape continues to experience significant demand. In 2023, 5% of all net new assets into U.S.-listed ETFs was absorbed by an ETF with a Buywrite option overlay strategy.<sup>1</sup> This trend has continued into early 2024.<sup>2</sup>*

*One iteration of the Buywrite is a covered call & growth strategy. This strategy seeks to achieve a dual objective of option premium income paired with some upside potential on the long reference asset. Even as interest rates remain elevated, equity income is in demand. Investors may find an equity-based covered call & growth strategy as a palatable core complement or as a replacement to factor-based dividend strategies, which can skew a portfolio's equity sector and style box exposures. In this piece, we'll detail how Global X's flagship covered call & growth ETFs, the Nasdaq 100 Covered Call & Growth ETF (QYLG) and the S&P 500 Covered Call & Growth ETF (XYLG), may serve as reasonable portfolio additions.*

## Key Takeaways

- The strategies employed by QYLG and XYLG are structured to maintain long exposure to a well-known stock index, the Nasdaq 100 and S&P 500 respectively, while writing covered calls on half of the portfolio's notional exposure. This type of strategy may simplify the allocating process and serve as a replacement to equity dividend strategies.
- Equity dividend strategies come equipped with some potential drawbacks, including isolated exposure to specific market sectors. Implementation of an index-based call writing strategy might help alleviate this concern by taking on an income generation role within a portfolio.
- Although interest rates remain elevated, the call option premiums generated by Buywrite ETF strategies have helped promote high income potential, keeping them in demand. Conversely, dividend ETF flows have dwindled, in comparison.

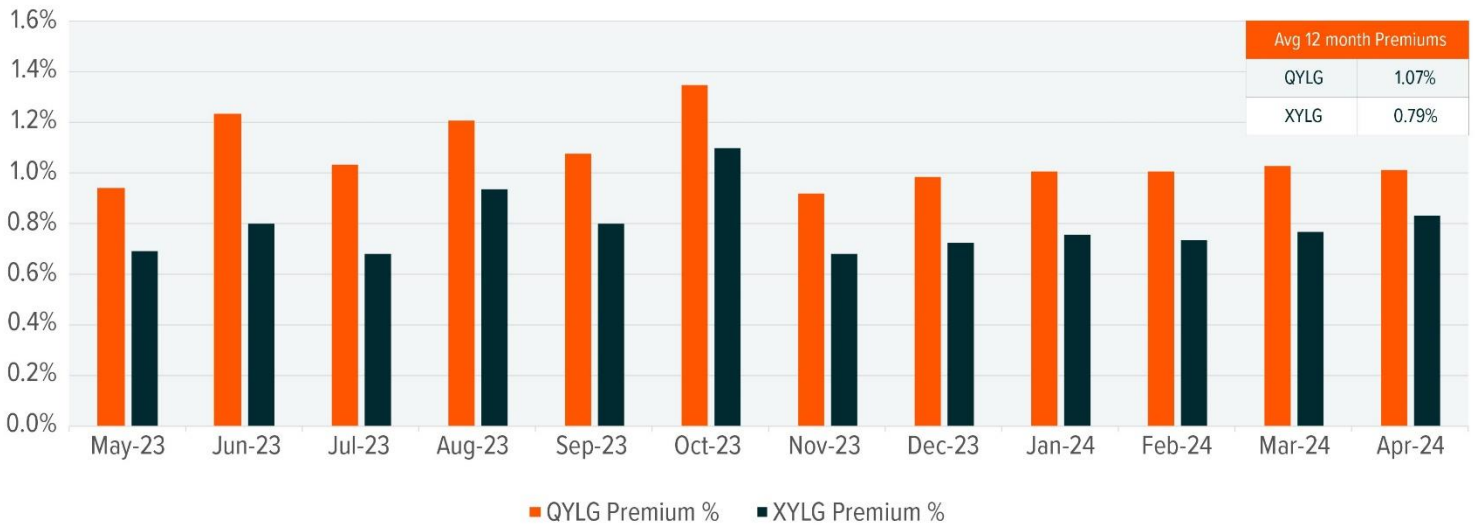
## Understanding Global X's 50% Covered Call Strategies Place in the Equity Income ETF Landscape

The equity-based ETF landscape has evolved and systematic options selling strategies, like QYLG and XYLG, have grown to represent a core piece. Both ETFs implement a covered call & growth strategy by writing "at-the-money" (ATM), cash-settled, index call options monthly on 50% of their respective stock portfolios while leaving the remaining 50% of the portfolio uncovered. The expectation is that each ETF can achieve half of the upside potential of its respective underlying index while its systematic monthly options writing strategy can create a stream of income through the distribution of half its premiums received up to 1% of net asset value.



# QYLG & XYLG'S CALL WRITING STRATEGY GENERATES MONTHLY PREMIUMS FOR INCOME POTENTIAL

Source: Global X ETFs. Data measured from May 19th, 2023 to April 19th, 2024.



Implied volatility, which historically has a positive correlation with option prices, has trended to historically low levels, of late.<sup>3</sup> However, by writing their call options “at-the-money”, option premium potential increases, since call options increase in value the closer the strike price of the contract is to the market price of the reference index at contract initiation. Recently, this component has enabled both ETFs to offer competitive yields relative to well-known U.S. dividend income indexes. In fact, year to date, as of 03/31/2024, both ETFs have outperformed the S&P 500 High Dividend and S&P 500 Dividend Aristocrats indexes. Over the last three years, XYLG has outperformed both indexes on a risk-adjusted basis when analyzing sortino ratios, a data point measuring returns for each unit of downside risk.

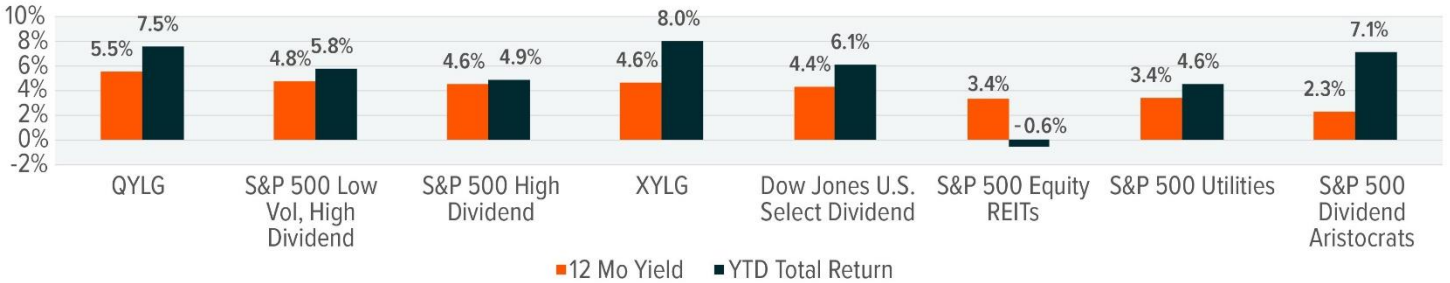


# EQUITY BASED INCOME LANDSCAPE OVERVIEW

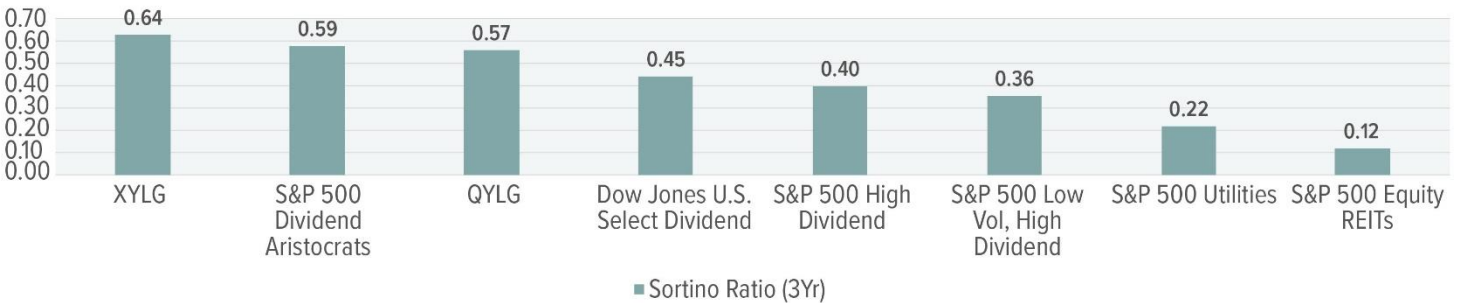
Sources: Global X ETFs with information derived from Morningstar Direct. Data as of March 31st, 2024.

Asset Class representations are as follows: S&P 500 Low Vol, High Dividend, S&P 500 Low Volatility High Dividend Index; S&P 500 Equity REITs, Real Estate Select Sector Index; S&P 500 Utilities, Utilities Select Sector Index. ETF and index yield are represented by 12-month trailing yields. QYLG & XYLG returns are based on NAV returns.

### U.S. Equity Income Landscape Overview



### Sortino Ratio (3Yr)



*Past performance is not a guarantee of future results. Past performance does not guarantee future results. The investment return and principal value of an investment will fluctuate so that an investor's shares, when sold or redeemed, may be worth more or less than their original cost and current performance may be lower or higher than the performance quoted. High short-term performance, when observed, is unusual and investors should not expect such performance to be repeated. For performance current to the most recent month- or quarter-end or a copy of the Fund prospectus, please visit [QYLG](#) and [XYLG](#).*

## Equity Dividend Strategies May Increase Sector & Style Risks

By maintaining underlying equity exposures that track the S&P 500 and Nasdaq 100, respectively, XYLG and QYLG grant investors the opportunity to diversify away from the value-oriented companies that are typically associated with dividend-targeted accounts. These include companies that exist in cyclical industries such as financials and materials, as well as defensive sectors like consumer staples and utilities. While equity dividend strategies may offer a defensive sector tilt, the reception of call premiums may play a defensive role for the Global X covered call & growth ETFs.

Presently, the average dividend ETF is underweight the information technology sector by a 19% margin relative to the S&P 500, and by a far wider gap versus the Nasdaq 100. As a consequence to this, these same strategies, on average, are underweight large cap equities, potentially increasing small and mid-cap size equity risks within an income allocation. By seeking to fill out the income arm of an equity portfolio with premium income through an S&P 500 or Nasdaq 100 covered call strategy as opposed to dividend income, however, more of an interest in sectors characterized as growth might be attained.



## DIVIDEND INVESTORS MAY BE UNDERWEIGHTING KEY GROWTH SECTORS

Sources: Global X ETFs with information derived from Morningstar Direct. Data as of March 31st, 2024. Average U.S. equity dividend ETF sector exposure was calculated using 59 dividend ETFs classified as a dividend strategy under Morningstar's Strategic Beta Groups.

### Sector Exposure

Sector	Average Dividend ETF	S&P 500 Index	Nasdaq 100 Index
Information Technology	10.3%	29.6%	49.8%
Communication Services	3.7%	9.0%	15.5%
Consumer Discretionary	8.2%	10.3%	13.0%
Consumer Staples	11.2%	6.0%	6.4%
Healthcare	9.3%	12.4%	6.3%
Industrials	11.9%	8.8%	4.8%
Materials	5.8%	2.4%	1.6%
Utilities	9.1%	2.2%	1.2%
Financials	17.5%	13.2%	0.5%
Energy	8.5%	3.9%	0.5%
Real Estate	4.5%	2.3%	0.3%

### Style Box Exposure

Style Box	Average Dividend ETF	S&P 500 Index	Nasdaq 100 Index
Large Cap Core	14.7%	31.3%	31.8%
Large Cap Growth	4.5%	34.5%	51.1%
Large Cap Value	22.0%	16.0%	6.8%
Mid Cap Core	12.9%	9.3%	4.5%
Mid Cap Growth	1.6%	3.0%	3.5%
Mid Cap Value	20.2%	5.6%	2.3%
Small Cap Core	8.0%	0.2%	0.0%
Small Cap Growth	1.8%	0.0%	0.0%
Small Cap Value	14.2%	0.2%	0.0%

## Equity Markets are Catching the Buywrite ETF Adoption Wave

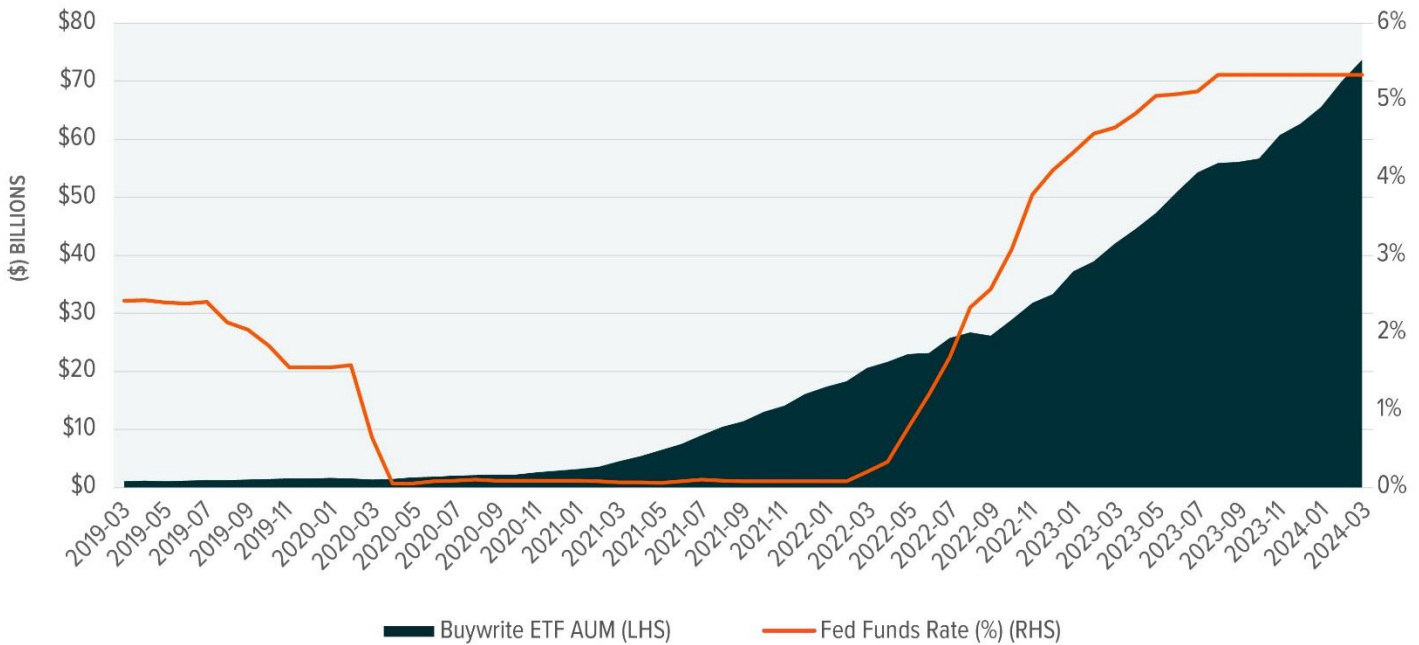
Buywrite ETFs have been made available to the public for more than a decade. However, the exponential growth story that they've developed of late was only recently catalyzed by the Federal Reserve's zero-interest rate policies ("ZIRP") of the COVID-19 era. In that environment, the yield-to-worst on U.S. high yield bonds fell to a 10-year low 3.75% by June of 2021.<sup>4</sup> With credit failing to fully address the void, alternative avenues through which to attain current income, like Buywrite strategies, were able to pick up the slack and thrive. Dividend investing experienced similar demand, taking in more net new assets than any single-factor strategy over the last three years (\$108B).<sup>5</sup>



This dynamic has changed, however, while investor demand for income has not. Over the last twelve months, Buywrite ETFs have experienced \$26B in net flows versus a relatively meager \$3B in net flows for dividend ETFs.<sup>6</sup> Part of this is due to the elevated income potential that may be offered by such option strategies. Expansion also stems from the potential for investors to map core equity exposures more efficiently.

## HIGHER INTEREST RATES HAVE NOT SLOWED DOWN BUYWRITE ETF MARKET GROWTH

Sources: Global X ETFs with information derived from Morningstar Direct. U.S. listed ETFs operating buywrite strategies defined using Global X's proprietary fund classification system. Data measured monthly from March 31st, 2019 to March 31st, 2024.



### Covered Call & Growth Can Replace a Dividend Holding

Dividend investing has historically represented a core component of income-oriented equity portfolios. However, the opportunity to keep the equity sleeve simple and potentially diversify not only underlying equity holdings, but also the very streams of income that support broader portfolios has become difficult to ignore. The S&P 500 and Nasdaq 100 indices have increasingly become a bedrock to core equity index investing. Combined, there are \$3.2T in assets under management tied to long-only ETFs and mutual funds that track these indices, representing 24% of all U.S. equity ETF and MF assets under management.<sup>7</sup> By allocating to these same baskets of stocks through QYLG and XYLG, the portfolio allocation process for income investors who already invest in another investment fund that offers similar exposure may become easier and reduce exposure disruptions.

#### Related ETFs

[QYLG – Global X Nasdaq 100 Covered Call & Growth ETF](#)

[XYLG – Global X S&P 500 Covered Call & Growth ETF](#)

*Click the fund name above to view current performance and holdings. Holdings are subject to change. Current and future holdings are subject to risk.*

#### Footnotes

1. Global X and Morningstar Direct. Funds operating buywrite strategies defined using Global X's proprietary fund classification system. Information measured from January 1, 2023 to December 31, 2023. Retrieved April 17, 2024.
2. Global X and Morningstar Direct. Funds operating buywrite strategies defined using Global X's proprietary fund classification system. Information measured from January 1, 2024 to March 31, 2024. Buywrite ETFs have grown at an 11.88% organic growth rate year-to-date. Retrieved April 17, 2024.





- Global X with information derived from Morningstar Direct. Measured from April 1, 2014 to March 31, 2024, the median Cboe Volatility Index (VIX) level was 16.06. As of March 31<sup>st</sup>, 2024, the level of the VIX was 13.01. Over the same timeframes, the median Cboe Nasdaq 100 Volatility Index (VXN) level was 19.55 and 16.66. Retrieved April 17, 2024.
- Global X with information derived from Morningstar Direct. Measured monthly from March 2014 to March 2024 using yield-to-worst measurements of the Bloomberg US Corporate High Yield Bond Index. Retrieved April 17, 2024.
- Global X with information derived from Morningstar Direct. Measured monthly from March 2021 to March 2024 using ETFs classified as a Dividend strategy under Morningstar's Strategic Beta Groups. Retrieved April 17, 2024.
- Global X with information derived from Morningstar Direct. Measured monthly from March 2023 to March 2024 using ETFs classified as a Buywrite strategy under Global X's proprietary fund classification system and ETFs classified as a Dividend strategy under Morningstar's Strategic Beta Groups. Retrieved April 17, 2024.
- Global X and Morningstar Direct. Measured as of March 31<sup>st</sup>, 2024. Retrieved April 17, 2024.

## Glossary

**S&P 500 Index:** S&P 500 Index tracks the performance of 500 leading U.S. stocks and captures approximately 80% coverage of available U.S. market capitalization. It is widely regarded as the best single gauge of large-cap U.S. equities.

**Nasdaq 100 Index:** The Nasdaq-100 Index includes 100 of the largest domestic and international non-financial companies listed on The Nasdaq Stock Market based on market capitalization. The Index reflects companies across major industry groups including computer hardware and software, telecommunications, retail/wholesale trade and biotechnology. It does not contain securities of financial companies including investment companies.

**Cboe Volatility Index (VIX):** Reflects a market estimate of future volatility of the U.S. stock market, based on the weighted average of implied volatilities of the S&P 500.

**Cboe Nasdaq 100 Volatility Index (VXN):** Reflects a market estimate of future volatility of the Nasdaq 100 index, based on the weighted average of implied volatilities of the Nasdaq 100.

**S&P 500 High Dividend Index:** The S&P 500 High Dividend Index serves as a benchmark for income seeking equity investors. The index is designed to measure the performance of 80 high yield companies within the S&P 500 and is equally weighted to best represent the performance of this group, regardless of constituent size.

**S&P 500 Dividend Aristocrats Index:** S&P 500® Dividend Aristocrats® measure the performance of S&P 500 companies that have increased dividends every year for the last 25 consecutive years. The Index treats each constituent as a distinct investment opportunity without regard to its size by equally weighting each company.

**S&P 500 Low Volatility High Dividend Index:** measures the performance of the 50 least-volatile high dividend-yielding stocks in the S&P 500.

**Dow Jones U.S. Select Dividend Index:** The Dow Jones U.S. Select Dividend Index aims to represent the U.S.'s leading stocks by dividend yield.

**Real Estate Select Sector Index:** All components of the S&P 500® are assigned to one of the eleven Select Sector Indices, which seek to track major economic segments and are highly liquid benchmarks. Real Estate stock classifications are based on the Global Industry Classification Standard (GICS®). Capping is applied to ensure diversification among companies within each index.

**Utilities Select Sector Index:** All components of the S&P 500® are assigned to one of the eleven Select Sector Indices, which seek to track major economic segments and are highly liquid benchmarks. Utilities stock classifications are based on the Global Industry Classification Standard (GICS®). Capping is applied to ensure diversification among companies within each index.

**Buywrite Strategy:** an options strategy where an investor sells (writes) a call option on the same asset they already own.

**12 Month Yield:** A calculation that divides a fund's cumulative distributions over the trailing 12-month period by its net asset value at the end of the period to determine a yield associated with holding a position in the fund over that time frame.

**Sortino Ratio:** Measures the return for each unit of downside risk. The risk-free rate is subtracted from the annualized return and is divided by the downside deviation of returns.

**Yield to Worst:** A measure of the lowest possible yield that can be received by a bond that could potentially possess an early retirement provision.

**Strategic Beta Group:** A classification of the overall strategy being employed by a fund as a result of its selection and weighting process with the intention to help investors home in on groups of funds with similar investment objectives.

**Dividend Strategic Beta Group:** A group for strategic-beta products which seek to deliver equity income by employing a number of dividend-related screening and/or weighting criteria.

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This material represents an assessment of the market environment at a specific point in time and is not intended to be a forecast of future events, or a guarantee of future results. This information is not intended to be individual or personalized investment advice and should not be used for trading purposes. Please consult a financial advisor for more information regarding your situation.

Investing involves risk, including the possible loss of principal. Concentration in a particular industry or sector will subject QYLG and XYLG to loss due to adverse occurrences that may affect that industry or sector. Investors in QYLG and XYLG should be willing to accept a high degree of volatility in the price of the fund's shares and the possibility of significant losses.

QYLG and XYLG engage in options trading. An option is a contract sold by one party to another that gives the buyer the right, but not the obligation, to buy (call) or sell (put) a stock at an agreed upon price within a certain period or on a specific date. A covered call option involves holding a long position in a particular asset and writing a call option on that same asset with the goal of realizing additional income from the option premium. By selling covered call options, the fund limits its opportunity to profit from an increase in the price of the underlying index above the exercise price, but continues to bear the risk of a decline in the index. A liquid market may not exist for options held by the fund. While the fund receives premiums for writing the call options, the price it realizes from the exercise of an option could be substantially below the indices current market price. QYLG is non-diversified.

Shares of ETFs are bought and sold at market price (not NAV) and are not individually redeemed from the Fund. Brokerage commissions will reduce returns. Indices are unmanaged and do not include the effect of fees, expenses or sales charges. One cannot invest directly in an index.

**This material must be preceded or accompanied by the current prospectus. Please read it before investing.**

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The Global X Derivative Strategy Classification System is based on the expertise, views, and opinions of the Global X Derivative Strategy Classification Committee and are subject to change. Global X defines thematic investing as the process of identifying powerful disruptive macro-level trends and the underlying investments that stand to benefit from the materialization of those trends. By nature, thematic investing is a long term, growth-oriented strategy, that is typically unconstrained geographically or by traditional sector/industry classifications, has low correlation to other growth strategies, and invests in relatable concepts.

The process to identify a derivative-based strategy incorporates three main principles:

The product must utilize derivatives as a core component of its investment strategy. This does not necessarily mean that derivatives must make up the majority of the ETF's portfolio. However, derivatives must serve a key purpose in achieving the investment objective stated in the ETF's prospectus.

The derivative-based strategy can be utilized over a long-term period from the standpoint that it is able to be used tactically, for temporary exposure to express a market view, or within a strategic allocation. Strategies whose core objective is to be a daily trading tool will most likely not be considered for inclusion.

The strategy must use derivatives as a means to achieve 1 or more of the 3 main use cases of derivatives by either buying or selling short a specific type of derivative:

**Risk Management** – These are strategies with an objective of achieving higher risk-adjusted returns by lowering overall portfolio volatility with the usage of derivatives.

**Income** – Strategies that utilize derivatives as a core investment to potentially achieve high income for its investors.

**Performance Enhancement** – Strategies that use derivatives to enhance the upside potential for capital appreciation, typically increasing the economic leverage used within a portfolio.

Taking the above principles into account, it should be noted that the derivative-based classification system does not consist of leveraged/inverse ETFs whose core objective is to track an index that rebalances daily. This goes against the 2nd principle stated above regarding the strategy being a long-term investment. Based on the definitions and principles described above, the derivative-based classification system is organized into multiple layers for a more refined understanding as to the objective of each strategy. Note that some options strategies can be utilized for multiple purposes, whether that be for Income, Risk Management, or Performance Enhancement, resulting in some categories appearing more than one time. The system consists of four layers of classification: (1) Derivative Objective (2) Derivative Strategy (3) Derivative Overlay and; (4) Derivative Tactic.

'Derivative Objective' is the broadest layer and this gives an understanding as to the core objective of the fund, utilizing the 3 derivative use cases defined in the Principles section: (1) Risk Management, (2) Derivative Income, and (3) Performance Enhancement. One layer down is 'Derivative Strategy,' which will provide investors the means by which the investment objective is being pursued. For example, an ETF that utilizes derivatives with a Risk Management objective can be generated using either a Tail Risk Strategy to provide a level of downside protection or a Collar Strategy to provide a range-bound return outcome. Although slightly different, the commonality between these two overlays are the fact that their core purpose is to provide Risk Management.

Further down, we identify 'Derivative Overlay' as a layer describes the specific derivatives being used and the manner in which they are being used (Long or Short, Bull or Bear). For example, a Tail Risk overlay can obtain a level of downside protection using many kinds of derivatives. Some overlays include either "going-long" with put options via a Protective Put or harnessing VIX Futures as an overlay on an existing stock portfolio. Lastly, 'Derivative Tactic' help to communicate to investors any unique considerations regarding the options overlay being used. For example, a strategy offering a Synthetic Exposure are primarily meant to be exposure vehicles to. Another example is a Defined-Outcome ETF, which utilizes put spread collars to offer a specific level of downside protection with capped upside potential if held over the course of the stated "outcome-period", making each iteration different from one another.

The number of derivative objectives, derivative strategies, derivative overlays, and derivative tactics are expected to change as new derivative-based strategies come to market. These updates will be made by the Global X Derivative Strategy Classification Committee ("the committee") and take into account official fund prospectus filings as well as fund company materials.

The ETF industry is continually innovating to provide unique derivative exposures to investors. The Global X Derivative Strategy Classification Committee evaluates these innovations by first investigating if a fund aligns with the core three principles of what it believes a derivative strategy to be. Then, once a fund is deemed a "Derivative Strategy", the committee identifies what the core objective is, how this objective is being achieved, and what types of derivative positions are being utilized within the strategy by reviewing prospectuses, index methodologies (if applicable), stated objectives by the fund company, as well as underlying holdings. Once per month, the committee will review all new U.S.-Listed ETF launches to determine if the fund should be added and how it should be classified. In addition, the committee will also review any strategy changes that have occurred amongst existing ETFs within the Classification System that might merit reporting in the next monthly Derivative Strategy ETF Report.

While an ETF may engage in multiple objectives or strategies utilizing derivatives, the committee will determine the classification based on the true nature of the ETF.

While an ETF may be classified within a certain objective, strategy, overlay, or tactic, Global X does not give any assurances that the ETF provides good and accurate exposure to the specific exposure it is targeting. For example, an ETF may convey or market itself in a specific manner but still utilize a specific derivative trading strategy that has its own nomenclature.

The derivative classification system is reviewed monthly by the Global X Derivative Strategy Classification Committee to consider new changes and/or additions to the layers (categories) stated above. In addition, the committee will also seek to add newly launched, U.S.-listed ETFs that fit the 3 main principles of a derivative-based strategy.

In the event that an ETF changes its investment objective to another one that goes against the 3 principles of a derivative-based strategy, the strategy will be removed from the classification system and its historical assets under management data will be maintained within the monthly report. On the



other hand, if an ETF changes its investment objective to something that fits within the parameters of the 3 principles, it will be considered for inclusion in the classification system where its AUM will start to be reflected in the report.

Global X accepts requests for reviews or appeals for any ETFs. Please contact Global X at [research@globalxetfs.com](mailto:research@globalxetfs.com), and the appeal will be considered in a timely manner. There are no guarantees that an appeal will result in a change in the ETF's classification.

The Derivative-based ETF Report, including the classification system, falls under the supervision of the Global X Derivative-Based Strategy Classification Committee. The Committee consists of members from Global X's research and product teams who have extensive knowledge of the strategies themselves and the ETF industry. The goal of the committee is to properly identify and classify ETFs that fit the 3 principles. The Committee meets at least monthly to review the classification system, as well as on an ad-hoc basis to review new ETF launches or ETFs that change their strategy.

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