



GLOBAL X ETFs RESEARCH

Introducing the Global X Russell 2000 Covered Call & Growth ETF (RYLG)

Authored by:

Rohan Reddy
Director of Research

Date: October 5, 2022

Topic: **Income, Options, Risk Management**



Related ETFs

Please click below for fund holdings and important performance information.

[RYLG – Global X Russell 2000 Covered Call and Growth ETF](#)

On October 5th, we listed the [Global X Russell 2000 Covered Call & Growth ETF \(RYLG\)](#) on the New York Stock Exchange (NYSE). RYLG is the latest addition to Global X's covered call ETF suite, which is designed to offer investors both income and upside potential (though some may cap that potential). RYLG is the third fund in the Global X covered call & growth suite, which also has the [Global X Nasdaq 100 Covered Call & Growth ETF \(QYLG\)](#) and the [Global X S&P 500 Covered Call & Growth ETF \(XYLG\)](#). RYLG now brings Global X's options-based ETF suite to 15 funds in total.

With interest rates sitting at ultra-low levels for the past decade, income investors have struggled to find diversified sources of income for their portfolios. Traditional sources of income like equity and fixed income are still exhibiting yields well below inflationary levels, making it hard for these investors to generate real (inflation-adjusted) income. To combat this environment, investors have increasingly sought alternatives such as options strategies like covered calls that can offer income potential and long-term growth opportunities.

RYLG: A Russell 2000 Covered Call ETF Designed for Income and Growth Potential

- The Global X Russell 2000 Covered Call & Growth ETF (RYLG) buy the securities in the Russell 2000 at the respective weights in that index
- Each month, the ETF writes at-the-money (ATM) index call options on the Russell 2000 in an attempt to generate income
- The options written cover 50% of the value of the stocks held in the fund. This means the fund retains roughly half of the upside potential of the index

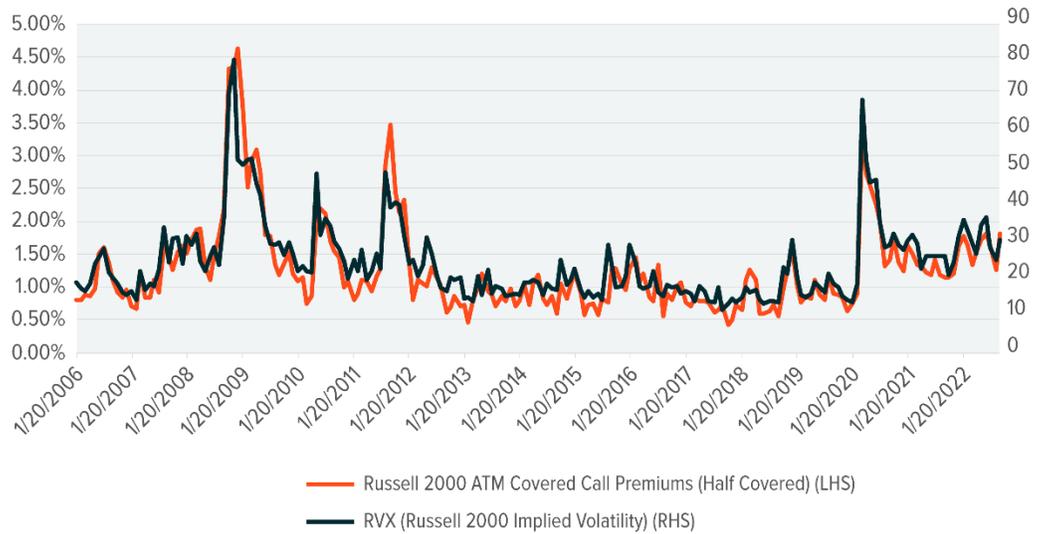
RYLG employs a covered call writing strategy in an effort to achieve both income and growth potential. The fund is passively managed and follows a rules-based approach. The fund also uses European style options which cannot be exercised until expiration and are also cash settled.

In the data tables included below, using a Black-Scholes options pricing model, we can see what the potential premiums on a strategy like this looks like using a 50% covered call Russell 2000 strategy going back the last 16 years, which includes periods like the global financial crisis.¹ In addition, we can also see the modeled premiums relative to the Russell 2000's implied volatility levels, which as expected, it closely tracks.



CALCULATED RUSSELL 2000 ATM COVERED CALL PREMIUMS (HALF COVERED) VS. THE CBOE RUSSELL 2000 VOLATILITY INDEX (RVX)

Sources: Global X ETFs with information derived from: CBOE Markets and Bloomberg, L.P. (n.d.). [RVX Index from January 20, 2006 to September 16, 2022] [Data set]. Data from 1/20/2006 to 9/16/2022 using the data from the 3rd Friday of each month, when the options are written. Premiums are a hypothetical measurement since it is an index. These are calculated options premiums using the Black Scholes options pricing model. Actual premiums may have varied.



For context, Global X also runs two other Covered Call & Growth strategies similar in nature to RYLG, but instead on the Nasdaq 100 & S&P 500. Those funds are QYLG and XYLG, respectively. Below we can see the live premiums history since those funds have been available in the market.



| DATE | QYLG | | XYLG | |
|-----------|---------------------------------|--------------|---------------------------------|--------------|
| | Monthly Distribution Cap: 0.50% | | Monthly Distribution Cap: 0.50% | |
| | Option Premium | Distribution | Option Premium | Distribution |
| Sept 2020 | 1.80% | - | 1.03% | - |
| Oct 2020 | 1.73% | 0.51% | 1.21% | 0.50% |
| Nov 2020 | 1.93% | 0.50% | 0.59% | 0.47% |
| Dec 2020 | 2.11% | 0.50% | 0.57% | 0.46% |
| Jan 2021 | 1.70% | 0.50% | 1.21% | 0.50% |
| Feb 2021 | 1.12% | 0.50% | 0.77% | 0.39% |
| Mar 2021 | 1.46% | 0.50% | 0.84% | 0.42% |
| Apr 2021 | 1.13% | 0.50% | 0.76% | 0.38% |
| May 2021 | 1.01% | 0.50% | 0.69% | 0.34% |
| Jun 2021 | 0.89% | 0.44% | 0.79% | 0.28% |
| Jul 2021 | 1.05% | 0.50% | 0.76% | 0.38% |
| Aug 2021 | 0.87% | 0.43% | 0.75% | 0.37% |
| Sept 2021 | 0.86% | 0.43% | 0.73% | 0.37% |
| Oct 2021 | 0.88% | 0.44% | 0.69% | 0.35% |
| Nov 2021 | 0.93% | 0.47% | 0.74% | 0.37% |
| Dec 2021 | 1.23% | 4.29% | 0.89% | 3.46% |
| Jan 2022 | 1.40% | 0.50% | 1.04% | 0.50% |
| Feb 2022 | 1.55% | 0.50% | 1.17% | 0.50% |
| Mar 2022 | 1.44% | 0.50% | 1.14% | 0.49% |
| Apr 2022 | 1.47% | 0.51% | 1.05% | 0.51% |
| May 2022 | 1.57% | 0.50% | 1.25% | 0.50% |
| Jun 2022 | 2.14% | 0.49% | 1.66% | 0.50% |
| Jul 2022 | 1.78% | 0.49% | 1.38% | 0.50% |
| Aug 2022 | 1.38% | 0.51% | 1.00% | 0.50% |

As a general guideline, the monthly distribution of QYLG, XYLG & RYLG is capped at the lower of: a) half of premiums received, or b) 0.5% of net asset value (NAV). The excess amount of option premiums received, if applicable, is reinvested into the fund. Year-end distributions can exceed the general guideline due to capital gains that are paid out at the end of the year.

However, each index has its own respective attributes, meaning it may be more relevant to consider the Global X Russell 2000 Covered Call ETF (RYLD), which employs a 100% ATM covered call writing strategy on the Russell 2000. These premiums are also put side by side relative to two funds using 100% ATM covered call writing strategies on the Nasdaq 100 and S&P 500 as well, QYLD and XYLD, respectively.

Although this may not be exactly the case in practice, we expect the premiums received by RYLG to be approximately half of what RYLD generates, given the 50% versus 100% call writing on the portfolio of underlying securities.



| DATE | GYLD | | XYLD | | RYLD | |
|----------|------------------------------|--------------|------------------------------|--------------|------------------------------|--------------|
| | Monthly Distribution Cap: 1% | | Monthly Distribution Cap: 1% | | Monthly Distribution Cap: 1% | |
| | Option Premium | Distribution | Option Premium | Distribution | Option Premium | Distribution |
| Dec 2018 | 1.62% | 0.81% | 0.63% | 0.87% | - | - |
| Jan 2019 | 2.21% | 1.00% | 0.66% | 0.50% | - | - |
| Feb 2019 | 1.66% | 0.83% | 0.43% | 0.50% | - | - |
| Mar 2019 | 1.81% | 0.89% | 0.42% | 0.50% | - | - |
| Apr 2019 | 1.61% | 0.78% | 0.25% | 0.50% | - | - |
| May 2019 | 1.89% | 0.94% | 0.54% | 0.50% | 1.88% | 0.94% |
| Jun 2019 | 1.90% | 0.94% | 0.50% | 0.50% | 1.76% | 0.88% |
| Jul 2019 | 1.50% | 0.73% | 0.26% | 0.50% | 1.42% | 0.53% |
| Aug 2019 | 2.37% | 1.00% | 0.89% | 0.50% | 2.66% | 1.00% |
| Sep 2019 | 1.56% | 0.78% | 0.28% | 0.50% | 1.67% | 0.85% |
| Oct 2019 | 1.56% | 0.77% | 0.35% | 0.50% | 1.55% | 0.67% |
| Nov 2019 | 1.68% | 0.83% | 0.38% | 0.50% | 1.85% | 0.99% |
| Dec 2019 | 1.40% | 0.70% | 0.21% | 0.50% | 1.29% | 0.65% |
| Jan 2020 | 1.68% | 0.83% | 0.33% | 0.50% | 1.52% | 0.77% |
| Feb 2020 | 2.30% | 1.00% | 0.51% | 0.50% | 1.87% | 0.94% |
| Mar 2020 | 4.41% | 1.00% | 3.92% | 0.50% | 5.07% | 1.00% |
| Apr 2020 | 3.62% | 1.00% | 2.46% | 0.50% | 6.04% | 1.00% |
| May 2020 | 3.71% | 1.00% | 2.26% | 0.49% | 5.59% | 0.99% |
| Jun 2020 | 2.70% | 1.00% | 1.54% | 0.50% | 4.38% | 1.00% |
| Jul 2020 | 3.31% | 1.00% | 1.49% | 0.50% | 3.99% | 1.00% |
| Aug 2020 | 2.32% | 1.00% | 1.74% | 0.88% | 2.35% | 1.00% |
| Sep 2020 | 3.39% | 1.00% | 2.13% | 1.00% | 2.64% | 1.00% |
| Oct 2020 | 3.54% | 1.00% | 2.54% | 1.00% | 3.27% | 1.00% |
| Nov 2020 | 2.36% | 1.00% | 1.95% | 0.98% | 3.06% | 1.00% |
| Dec 2020 | 2.46% | 1.01% | 1.81% | 0.87% | 2.75% | 1.01% |
| Jan 2021 | 3.27% | 1.00% | 2.44% | 1.00% | 3.32% | 0.99% |
| Feb 2021 | 2.29% | 1.00% | 1.55% | 0.76% | 3.14% | 1.00% |
| Mar 2021 | 2.88% | 1.00% | 1.76% | 0.88% | 3.06% | 0.99% |
| Apr 2021 | 2.18% | 1.00% | 1.50% | 0.75% | 2.70% | 1.00% |
| May 2021 | 2.02% | 1.00% | 1.38% | 0.69% | 2.38% | 1.00% |
| Jun 2021 | 1.78% | 0.87% | 1.59% | 0.79% | 2.28% | 0.98% |
| Jul 2021 | 2.02% | 0.87% | 1.38% | 0.69% | 2.64% | 0.99% |
| Aug 2021 | 1.64% | 0.82% | 1.50% | 0.75% | 2.54% | 1.00% |



| DATE | QYLD | | XYLD | | RYLD | |
|-----------|------------------------------|--------------|------------------------------|--------------|------------------------------|--------------|
| | Monthly Distribution Cap: 1% | | Monthly Distribution Cap: 1% | | Monthly Distribution Cap: 1% | |
| | Option Premium | Distribution | Option Premium | Distribution | Option Premium | Distribution |
| Sept 2021 | 1.70% | 0.83% | 1.54% | 0.75% | 2.24% | 1.00% |
| Oct 2021 | 1.74% | 0.87% | 1.39% | 0.69% | 2.00% | 0.98% |
| Nov 2021 | 1.95% | 0.98% | 1.44% | 0.72% | 2.14% | 0.99% |
| Dec 2021 | 2.43% | 2.25% | 1.83% | 0.91% | 2.82% | 1.27% |
| Jan 2022 | 2.76% | 0.99% | 2.09% | 1.00% | 3.04% | 0.99% |
| Feb 2022 | 3.03% | 1.01% | 2.38% | 1.02% | 2.84% | 1.00% |
| Mar 2022 | 2.83% | 1.00% | 2.26% | 1.00% | 2.50% | 1.01% |
| Apr 2022 | 2.94% | 1.00% | 2.09% | 1.01% | 2.66% | 1.00% |
| May 2022 | 3.12% | 1.01% | 2.51% | 1.01% | 2.78% | 1.01% |
| Jun 2022 | 4.27% | 1.00% | 3.32% | 1.00% | 3.86% | 1.00% |
| Jul 2022 | 3.62% | 1.00% | 2.75% | 1.01% | 3.75% | 1.02% |
| Aug 2022 | 2.78% | 1.00% | 2.01% | 0.99% | 2.58% | 0.99% |

As a general guideline, the monthly distribution of QYLD, XYLD, RYLD & DJIA is capped at the lower of: a) half of premiums received, or b) 1% of net asset value (NAV). The excess amount of option premiums received, if applicable, is reinvested into the fund. Year-end distributions can exceed the general guideline due to capital gains that are paid out at the end of the year.

Covered Call ETFs Designed for Income and Growth Potential

RYLG uses covered call writing on half of its portfolio in an effort to achieve both income and growth. RYLG has a similar strategy to the other covered call and growth strategies in our suite, QYLG and XYLG, just focused on a different index. Similarly, our covered call and growth strategies are similar to our covered call strategies in that they write covered calls in an effort to provide income. The primary difference between RYLG and RYLD is that RYLG writes options to cover 50% of its stock holdings, whereas RYLD covers 100%. Accordingly, RYLG may generate approximately 50% of the income of RYLD.

RYLG Coverage Percentage: Tradeoff between Growth and Income

Investors must consider multiple factors in deciding the specifics of a covered call strategy. One primary topic to consider is the amount of the portfolio that will be covered by call options.

An investor must choose whether to fully cover or only partially cover their underlying position. If the underlying position experiences a 1% gain:

- If an investor is fully covered, the fully covered investor would not partake in the gains
- If an investor is 50% covered, they would take in 50% of the upside

On the opposite side of this, if the underlying stock experiences a 1% decline:

- The fully covered investor would take part in the decline, but it would be partially offset by the premiums from the options that is received
- If an investor is 50% covered, they would participate in a greater proportion of the decline as the 50% covered investor only receives half of the premium amount to offset losses



VARYING COVERAGE OF LONG POSITION

| | 50% Coverage | 100% Coverage |
|-----------------------|--------------|---------------|
| UPSIDE POTENTIAL | Half | None |
| OPTION PREMIUM INCOME | Half | Full |

In a fully covered portfolio, the investor has no upside participation if the options are written at the money. Fully covered portfolios have written calls on 100% of the value of the underlying securities owned in the portfolio. However, because it is selling options at the underlying price, a fully covered strategy will typically generate income.

In an under covered portfolio, this means that the notional value of the written call options is less than that of the underlying portfolio. This allows the investor to participate in both some of the upside and some of the income. The tradeoff for the participation compared to the fully covered strategy is lower income. Thus, RYLG may be suited for investors who are looking for both growth and income potential.

Russell 2000 Characteristics & Performance

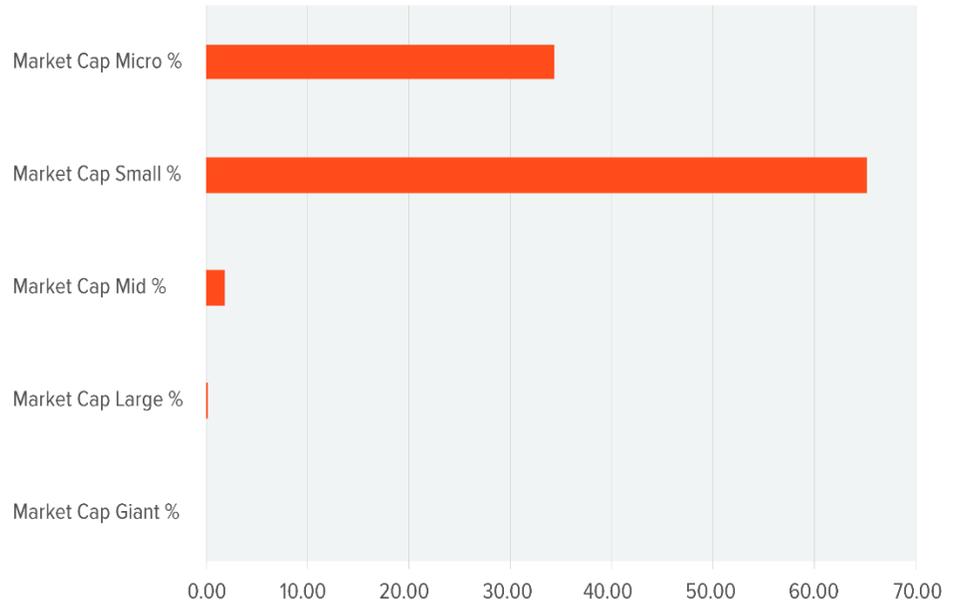
The Russell 2000 Index has performed well over the last decade due to the benefits of domestic revenue exposure, a strong dollar, US economic growth, and cheap financing conditions. The Russell 2000's outperformance over the S&P 500 Index can be attributed to the index's overweight towards value-oriented companies in the information technology and communication services sectors.

The Russell 2000 has a higher weight towards value oriented companies compared to the major US broad indices. The pure small cap exposure can also increase the overall volatility of index. This can be attributed to the fact that small cap companies are usually sensitive to rising rates for two main reasons. The first, being small cap companies tend to be considered a riskier investment leading to higher borrowing cost compared to the large cap counterpart. Second, many small cap companies are still in the early growth phase causing a higher need for debt and/or equity financing as they may not be producing sustainable cash flows, leading to a reinforced loop. However, small caps often have higher long term growth potential as they mature, which means investors may want to take part in some of that growth.



RUSSELL 2000 MARKET CAP BREAKOUT

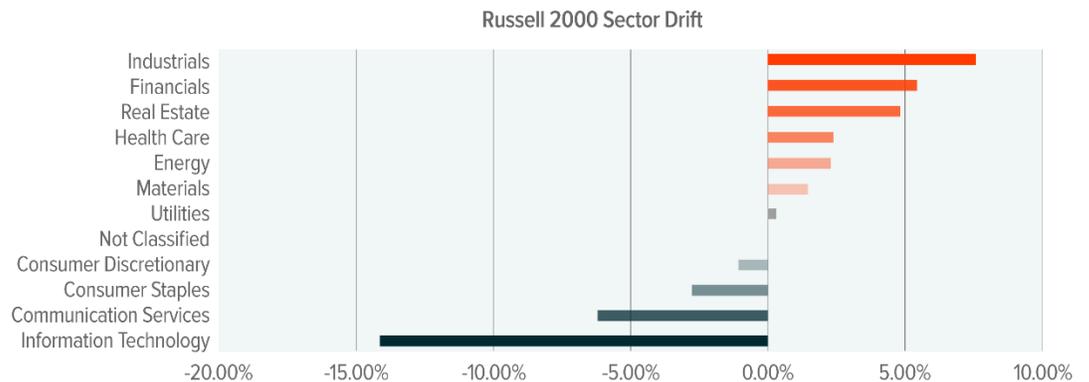
Sources: Global X ETFs with information derived from: Bloomberg, L.P. (n.d.). [Russell 2000 Market Cap breakout] [Data set]. Data as of and retrieved on September 30, 2022 from Global X Bloomberg terminal.



Higher rates reduce the present value of those distant cash flows which is something that is faced by technology and growth companies. While both segments have been negatively impacted, the decrease in price-to-earnings ratio associated with growth have been more pronounced compared to small caps, which have valuations that are more heavily based on near-term cash flows. The Russell 2000 Index has high exposure to Small-Cap Equities.

RUSSELL 2000 SECTOR DIFFERENCES (COMPARED TO S&P 500 INDEX)

Source: Global X ETFs with information derived from: Bloomberg, L.P. (n.d.). [Russell sector differences] [Data set]. Data as of and retrieved on August 4, 2022.



Using 50% Covered Call ETFs in a Portfolio

A 50% covered call strategy is designed to balance growth potential with income and allows investors to be aligned with both outcomes. Investors who are seeking to live off of their savings or are recently retired may want both current income and growth in an effort to fight off inflation. Investors who are more bullish and do not want to commit to a fully covered strategy could employ a 50% covered strategy to capture more upside potential.

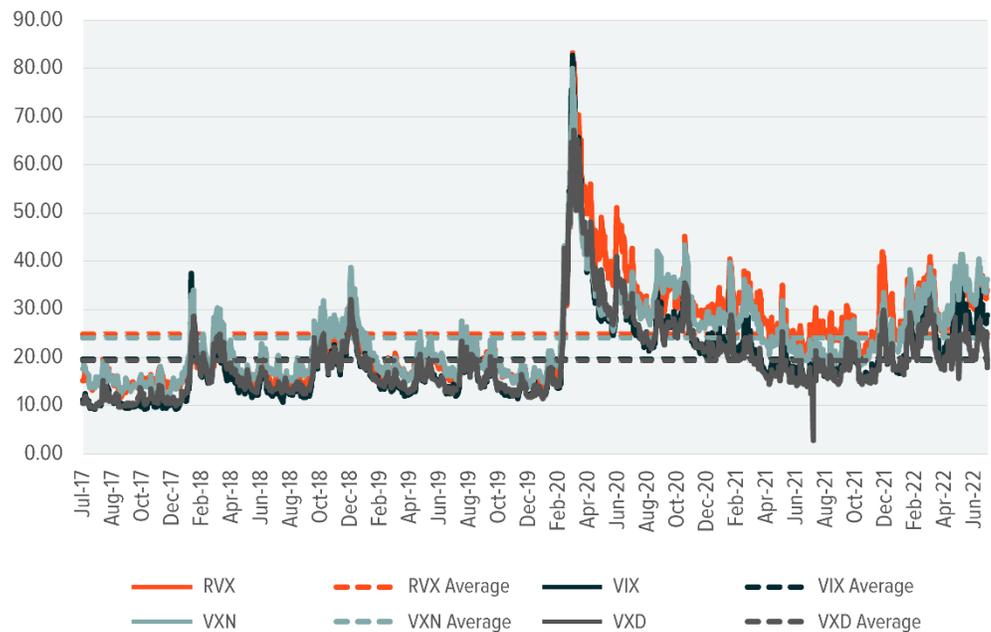
Additionally, investors who are seeking greater diversification for their portfolios may also prefer to have greater exposure to value oriented sectors, such as those in the Russell 2000. Having exposure to RYLG may allow investors to have greater weightings to sectors such as industrials, financials, and real estate.

Implementing a Russell 2000 Covered Call and Growth Strategy

Covered call and growth strategies such as RYLG could be valuable in an uncertain environment. Higher volatility tends to increase the options premiums received from selling calls, which can enhance returns even in a trendless market.

RUSSELL 2000 HAS RECENTLY PRODUCED HIGHER LEVELS OF VOLATILITY COMPARED TO THE S&P 500, NASDAQ 100, & DOW JONES INDUSTRIAL AVERAGE

Sources: Global X ETFs with information derived from: Bloomberg, L.P. (n.d.) [Russell 2000 volatility (as measured by CBOE Russell 2000 Volatility Index (RVX)) compared to S&P 500 volatility (as measured by CBOE Volatility Index (VIX)), NASDAQ 100 volatility (as measured by CBOE Nasdaq-100 Volatility Index (VXN)) and Dow Jones Industrial Average volatility (as measured by CBOE DJIA Volatility Index (VXD)) from July 1, 2017 to September 1, 2022] [Data set]. Data retrieved on September 1, 2022 from Global X Bloomberg terminal.



We can see above how the implied volatility of the Russell 2000 has been higher than the S&P 500, Nasdaq 100, and the Dow Jones Industrial Average, on average. This may result in higher relative premiums vs. large-cap indices signifying that harvesting small-cap premia may prove worthwhile for generating options income within a portfolio.



Using a 50% covered call strategy allows investors to express their bullish view on the market, while also getting half of the income as a fully covered call strategy on the same underlying assets. If options are appropriate for their portfolio, the decision for investors to choose between 100% covered and 50% covered depends on their investment objectives and current market views.

Investing in a covered call and growth fund may prove to be a more efficient option than individual investors implementing and managing covered call strategies on their own. An individual investor would need to buy the 2000 stocks in the Russell 2000 and then sell index call options each month. Buying the fund allows investors to outsource the responsibilities of managing the fund to a professional manager.

Today's current macroeconomic environment may prove to be well-suited for the 50% covered call approach on the Russell 2000. As income is challenging to find in many asset classes and with significant interest rate volatility but improved equity market performance, allowing for half of RYLG exposure to upside potential and the other half of RYLG exposure for generating income could prove to be an appealing solution for this market environment.

Footnotes

1. The Black Scholes model is a flagship model to calculate the fair price for an option contract using current stock price, expected dividends, strike price of an option, expected interest rates, time to expiration and expected volatility. The model assumes that dividends are not paid, the option can only be exercised at expiration, risk-free rate and volatility of the underlying investment are known and constant, no transaction costs are involved in buying the option, markets are efficient, and the returns are log-normally distributed.

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

RYLG engages 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. Investment in the Fund is subject to the risks of the underlying fund.

Diversification does not ensure a profit or guarantee against a loss.

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.

Carefully consider the funds' investment objectives, risks, and charges and expenses before investing. This and other information can be found in the funds' full or summary prospectuses, which may be obtained at globalxetfs.com. Please read the prospectus carefully before investing.

Global X Management Company LLC serves as an advisor to Global X Funds. The Funds are distributed by SEI Investments Distribution Co. (SIDCO), which is not affiliated with Global X Management Company LLC or Mirae Asset Global Investments. Global X Funds are not sponsored, endorsed, issued, sold or promoted by FTSE Russell or Cboe, nor do these entities make any representations regarding the advisability of investing in the Global X Funds. Neither SIDCO, Global X nor Mirae Asset Global Investments are affiliated with these entities.

