



# Enhancing the Hang Seng China Enterprises Index to Provide a Representative

## China Index of Hong Kong Market

17 August 2017



# The Consultation

- A consultation paper entitled “Proposal to enhance the Hang Seng China Enterprises Index as regards providing a representative China Index of Hong Kong Market” was issued on 3 March 2017.
- We consulted market participants from over 60 organisations, including fund managers, derivatives issuers and data products users.

Respondents	Number
Fund Managers	29
Derivatives Issuers	16
Data Product Users	4
Others	12
<i>Total</i>	<i>61</i>

# Definition of P-chips

All respondents supported adopting this definition as it is clear and more relevant from an investment perspective.

## Mainland Companies

Over 50% of the sales revenue (or profits or assets, if more appropriate) derived from mainland China



H-shares that have their primary listing on the Main Board of the SEHK

Yes



H-Shares

No



A minimum of 30% of shareholdings held by Mainland entities\*

Yes



Red-chips

No



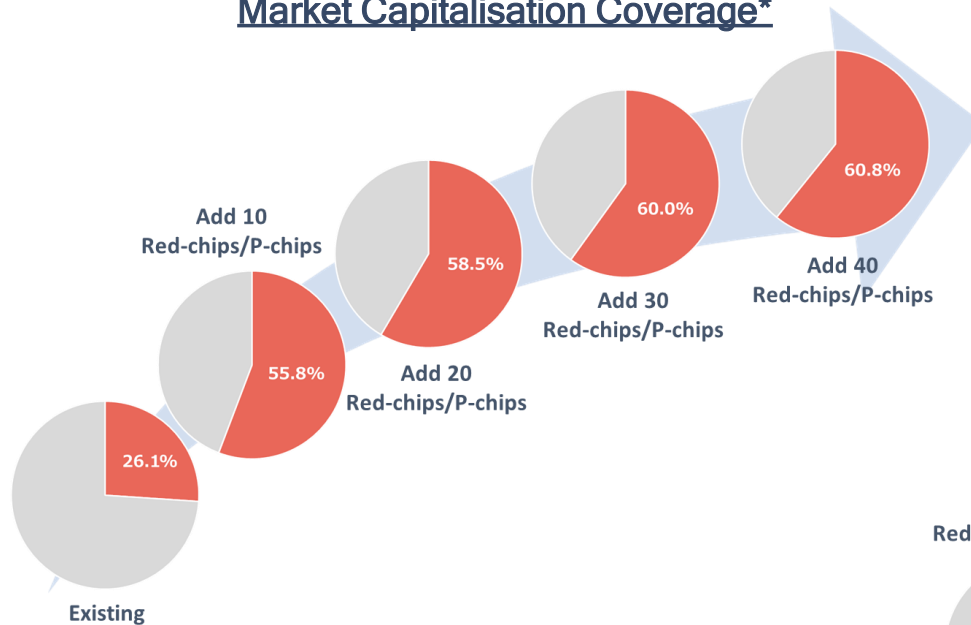
P-chips  
(Other Mainland Companies)

\*including state-owned organisations, provincial or municipal authorities of the Mainland

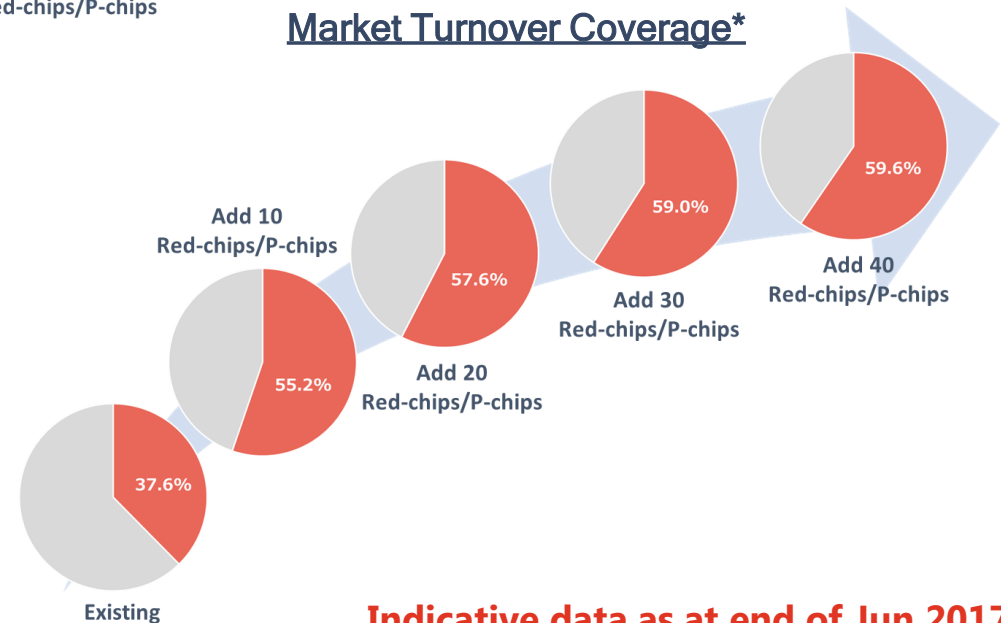
# Add Ten Red-chips/P-chips to the Index

Marginal benefit of adding more than 10 Red-chips / P-chips to the HSCEI is increasingly minimal.

## Market Capitalisation Coverage\*



## Market Turnover Coverage\*



\*Index coverage of all Main Board-listed Mainland companies as defined by Hang Seng Indexes

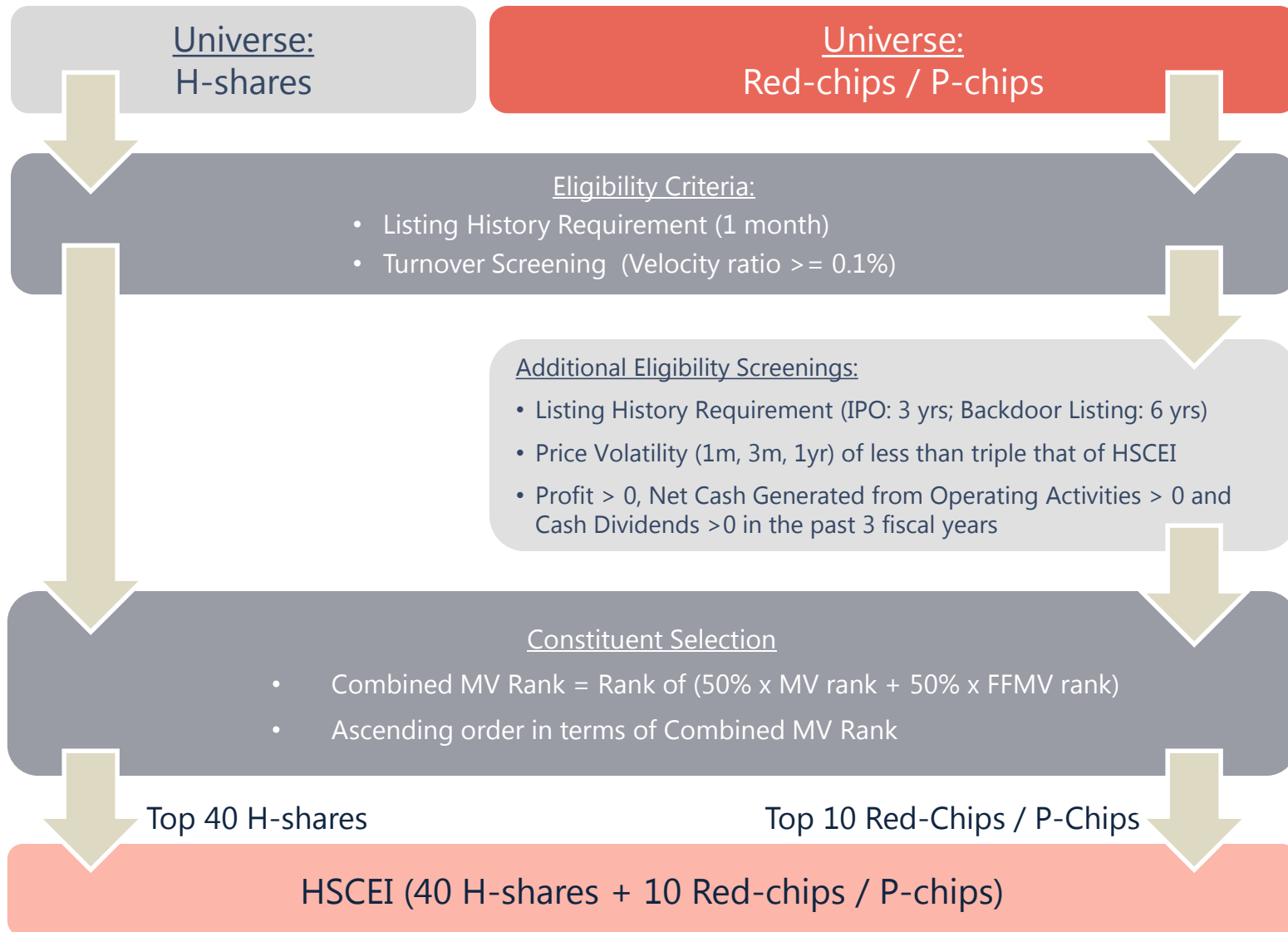
**Indicative data as at end of Jun 2017  
for illustration only**

# Additional Eligibility Screenings for Red-chips and P-chips

Almost all respondents supported imposing further screening and preferred highly transparent and rules-driven criteria.

Additional Eligibility Screenings	Requirements	Rationale
Listing History	<u>Three years</u> for companies listed through an IPO; or <u>Six years</u> for companies listed through a backdoor listing.	Sufficient audited financial records for reference
<b>AND</b>		
Price Volatility	The past one-month, three-month and 12-month historical price volatility of a potential constituent should not be more than <u>three times</u> the historical price volatility of the HSCEI for the respective period.	Avoid adding companies with very different risk profiles to the HSCEI
<b>AND</b>		
Financial	The following financial parameters of the company in the past three fiscal years must be <u>greater than zero</u> : <ul style="list-style-type: none"> <li>• Profit</li> <li>• Net Cash Generated from Operating Activities</li> <li>• Cash Dividends</li> </ul>	Avoid adding companies without consistent dividend payment records or non-profit-making companies to the HSCEI

# Application of New Methodology



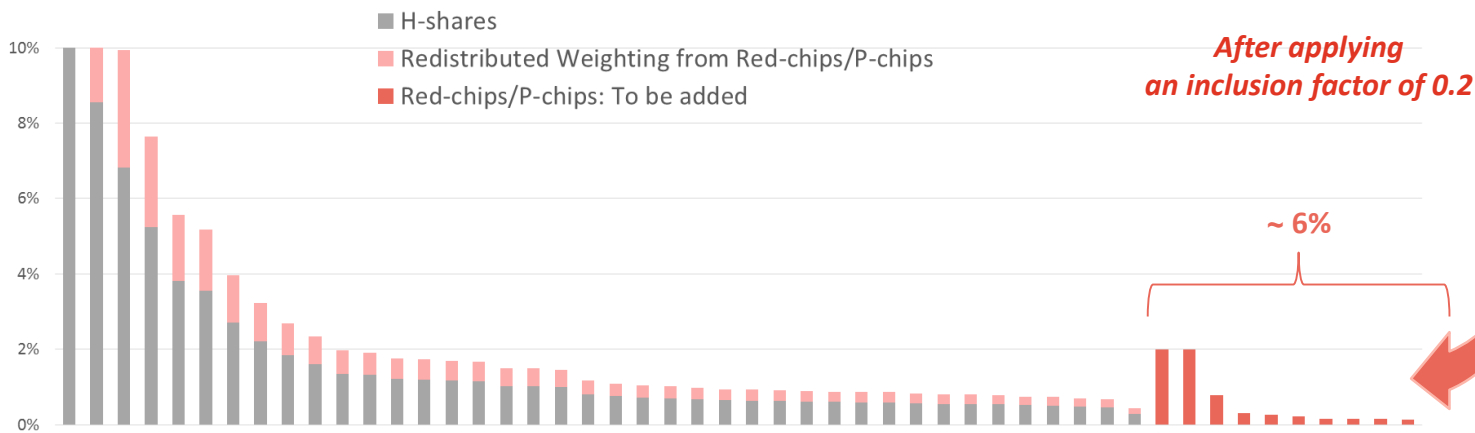
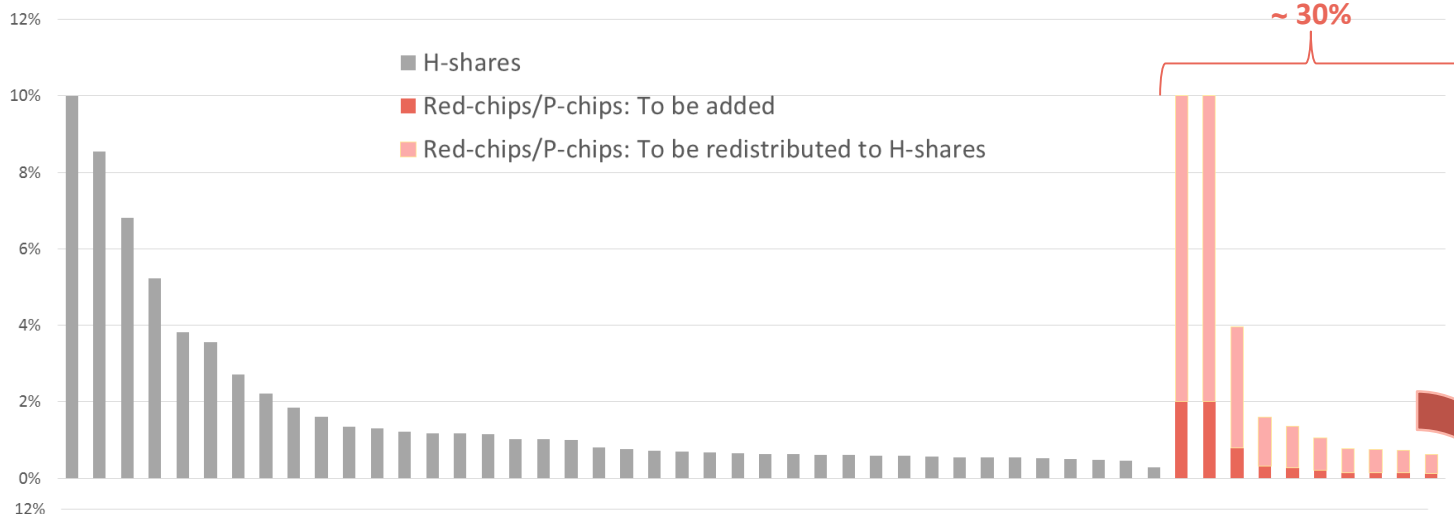
# Implement Changes in Five Phases

- The 10 Red-chips and P-chips constituents will be added to the HSCEI in five phases over a period of 12 months.
- The additional 10 constituents will be added to the HSCEI by adopting an inclusion factor and an adjusted cap level in each phase according to the following table:

Phase	Month*	Inclusion Factor	Adjusted Cap Level
1	March 2018	0.2	2%
2	June 2018	0.4	4%
3	September 2018	0.6	6%
4	December 2018	0.8	8%
5	March 2019	1.0	10%

\* The rebalancing date of regular index review. Exact dates will be announced in Feb 2018.

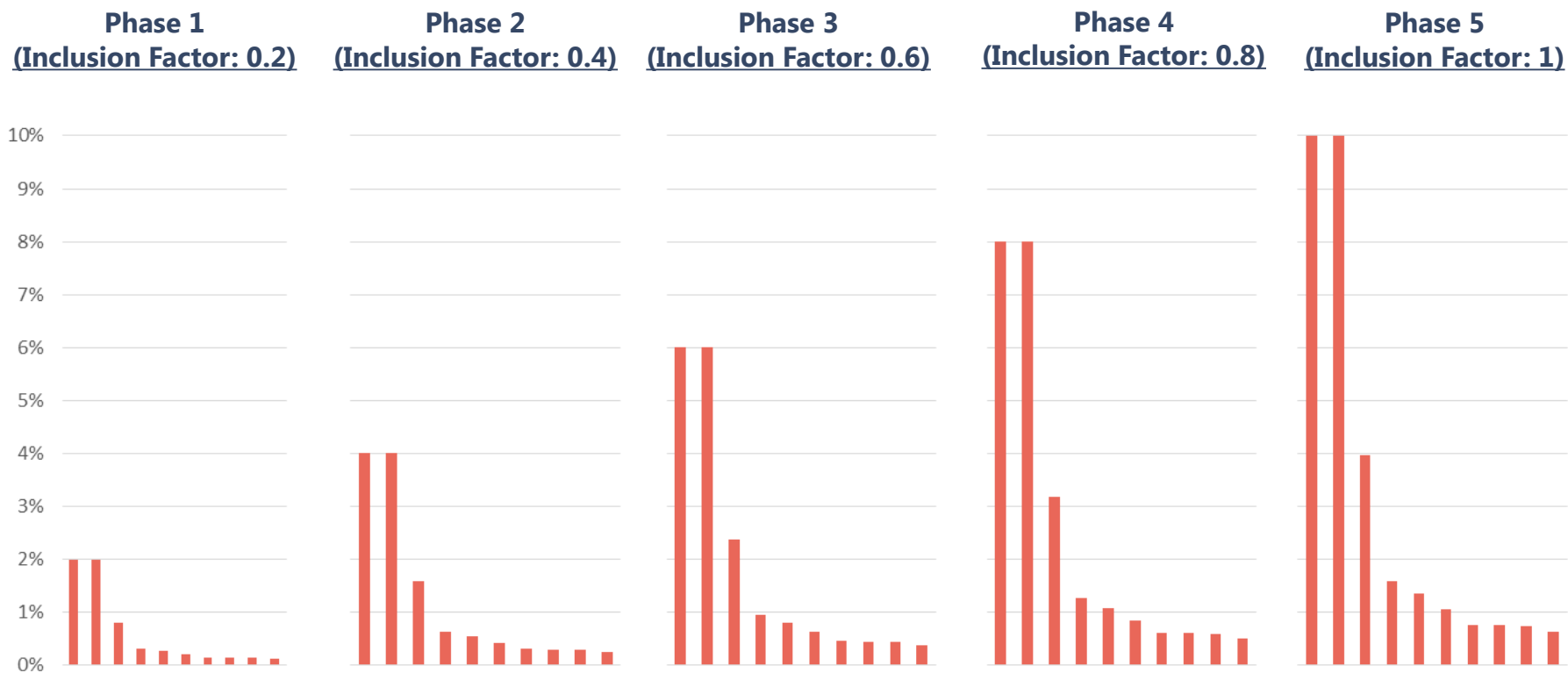
# Phase One - Indicative Index Weightings



**Indicative weighting as at end of Jun 2017  
for illustration only**

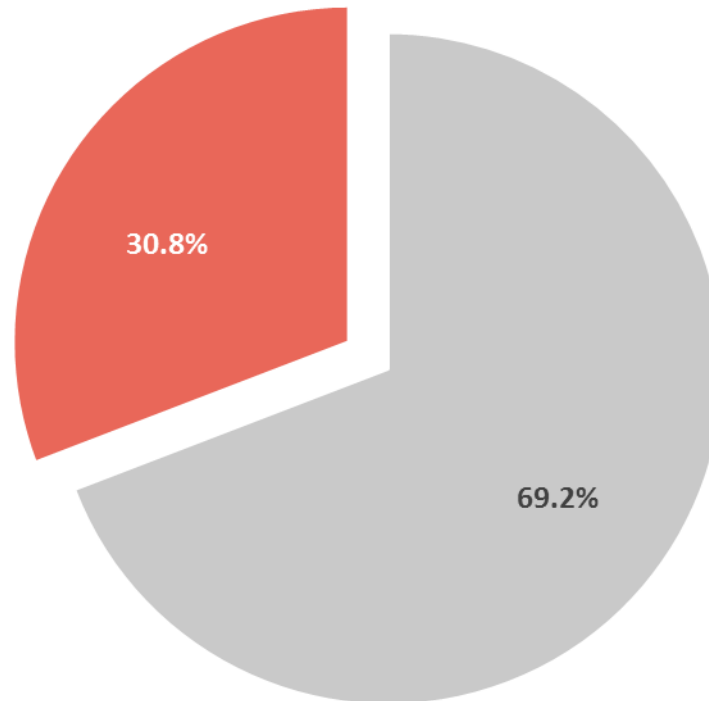


# Transition Through Phases - Indicative Index Weightings



**Indicative weighting as at end of Jun 2017  
for illustration only**

## Indicative index weighting

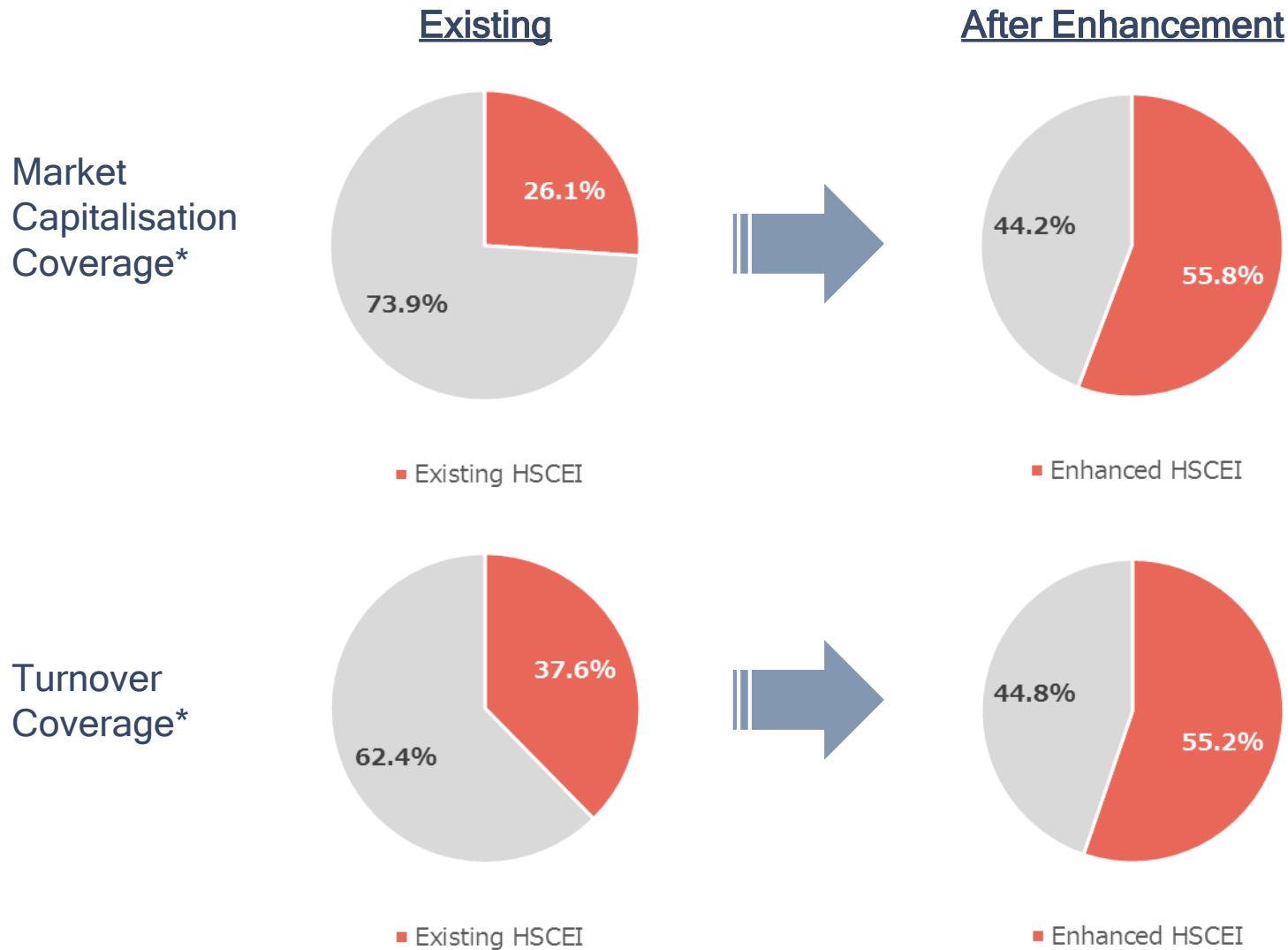


■ H-shares ■ Red-chips/P-chips

**Assume the transition has been completed**

**Indicative data as at end of Jun 2017 for illustration only**

# Indicative Coverage of the Enhanced HSCEI

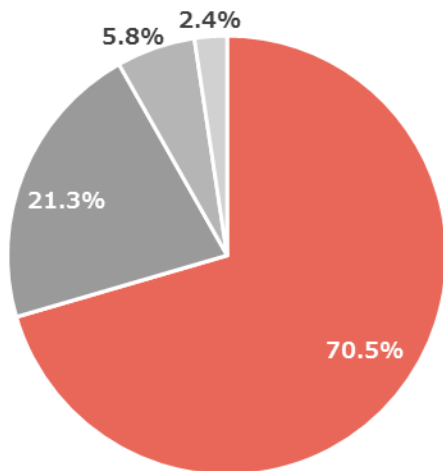


Assume the transition has been completed

Indicative data as at end of Jun 2017 for illustration only

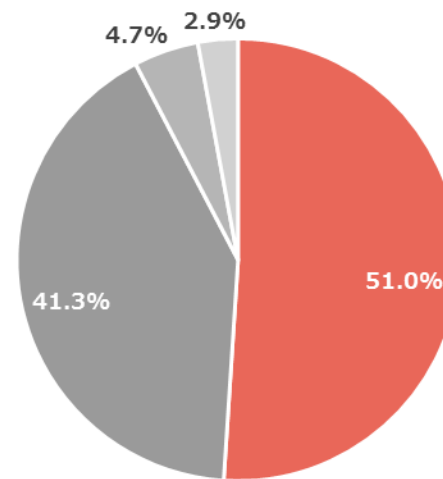
## Indicative index weighting

Existing



■ Finance ■ Commerce & Industry ■ Properties ■ Utilities

After Enhancement



■ Finance ■ Commerce & Industry ■ Properties ■ Utilities

**Assume the transition has been completed**

**Indicative data as at end of Jun 2017 for illustration only**

## ***Constituent Selection for H-shares to the Index***

- The number of H-shares constituents in the HSCEI will remain at 40 and the regular constituent change reviews will be conducted as usual.
- The constituent selection criteria for H-shares will remain unchanged.

## ***Constituent Selection for Red-chips and P-chips to the Index***

- The additional 10 Red-chips and P-chips for inclusion will be selected in the index review with a data cutoff of end-December 2017.
- The announcement will be made in February 2018 together with the regular index review results.
- It is intended that the 10 Red-chips and P-chips will remain unchanged for the whole transition period.

## ***After the Transition***

- Further announcement(s) will be made by end-2018 on the management of the HSCEI after the transition period.

# Changes to Other Derived Indexes

- All other indexes derived from the HSCEI will also be changed alongside the HSCEI.
- The relevant indexes are as follows:
  - Hang Seng China Enterprises Equal Weighted Index
  - Hang Seng China Enterprises Smart Index
  - Hang Seng Risk Adjusted Index – HSCEI 25%
  - Hang Seng Risk Adjusted Index (ER)– HSCEI 25%
  - Hang Seng China Enterprises Futures Index
  - Hang Seng China Enterprises Futures RMB FX Index
  - HSCEI Short Index
  - HSCEI 2x Short Index
  - HSCEI Leveraged Index

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