

S&P BSE Indices Consultation on Sector Diversification in Benchmark Indices

MUMBAI, MAY 22, 2019: On January 10, 2019, the Securities and Exchange Board of India (“SEBI”) issued a circular concerning portfolio concentration norms for equity exchange traded funds (“ETFs”) and index funds.¹ On April 9, 2019, Asia Index Private Limited (“AIPL”) announced changes to the index methodology of all applicable indices in order to adhere to these norms.²

Further to this, AIPL is seeking feedback from members of the investment community on the sector diversification of benchmark indices in India and whether limits, in the form of capping, should be considered.

For background, the table below summarizes the basic eligibility criteria for key benchmark indices in the S&P BSE index family:

Parameter	Methodology		
	S&P BSE 500	S&P BSE 100	S&P BSE SENSEX
Starting Universe	S&P BSE AllCap Index	S&P BSE LargeMidCap Index	S&P BSE 100
Liquidity	Stocks must have an annualized traded value of at least INR 1 billion (INR 800 million for current constituents).	Stocks must have an annualized traded value of at least INR 10 billion (INR 8 billion for current constituents).	Companies within the universe ranked among the top 75 by average six month float-adjusted or total market capitalization and having a cumulative annualized traded value within 98% are included.
Trading Frequency	Stocks must have traded on at least 80% of the trading days at the BSE during the six-month reference period.	Stocks must have no more than five non-trading days in the past six months, as of the rebalancing reference date.	Stocks must have traded on every trading day at the BSE during the six-month reference period.
Derivatives	--	The individual float-adjusted weight of any share class of a company not linked to derivatives trading cannot exceed 5% of the index. The aggregate float-adjusted weight of index constituents not linked to derivatives trading cannot exceed 10%.	--
Listing History	--	--	Stocks must have a listing history of at least six months at BSE.

For more information on the index methodology of the S&P BSE 500, S&P BSE 100, and S&P BSE SENSEX, please refer to the *S&P BSE Indices Methodology*, available [here](#).

¹ For details on the SEBI norms, please refer to SEBI circular no: SEBI/HO/IMD/DF3/CIR/P/2019/011 available [here](#).

² The full announcement is available [here](#).

Using the S&P BSE AllCap, a broad based index representing approximately 95% of the market capitalization of companies listed on the BSE, the tables below illustrate the evolution of sector representation in the Indian equity market over time.

S&P BSE AllCap – Sector Representation Over Time						
Sector	March 31					
	2019	2017	2015	2013	2011	2009
Finance	32.8%	28.0%	27.0%	25.6%	24.1%	18.6%
Consumer Discretionary Goods & Services	12.5%	13.7%	11.5%	10.1%	9.4%	7.8%
Information Technology	10.5%	9.4%	12.0%	11.7%	11.3%	9.0%
Energy	9.6%	8.8%	7.2%	10.3%	10.9%	16.7%
Fast Moving Consumer Goods	9.2%	9.3%	9.3%	12.1%	7.7%	9.1%
Industrials	8.5%	10.5%	12.3%	9.4%	12.8%	11.1%
Basic Materials	7.3%	8.1%	6.6%	7.9%	10.3%	9.0%
Healthcare	5.1%	6.5%	8.1%	6.2%	4.9%	5.1%
Utilities	3.0%	3.6%	3.4%	4.3%	5.9%	7.5%
Telecom	1.4%	1.7%	2.4%	2.0%	2.6%	5.9%
Diversified	0.2%	0.3%	0.3%	0.2%	0.2%	0.3%

The largest four sectors in the S&P BSE AllCap account for approximately 65% of the index weight by market cap. The table below shows the evolution of sector representation, based on size classification, over time.

S&P BSE AllCap – Sector Representation Based On Size Classification Over Time									
Sector	Large Cap – March 31			Mid Cap – March 31			Small Cap – March 31		
	2019	2015	2011	2019	2015	2011	2019	2015	2011
Finance	36.9%	28.4%	26.1%	29.0%	22.1%	19.5%	12.7%	8.0%	8.1%
Consumer Discretionary Goods & Services	8.7%	7.5%	5.7%	21.5%	25.1%	19.5%	26.1%	23.7%	22.0%
Information Technology	12.4%	15.6%	13.7%	2.9%	4.6%	4.7%	5.9%	8.3%	9.6%
Energy	12.2%	9.3%	14.1%	1.3%	1.3%	2.7%	1.7%	1.8%	2.2%
Fast Moving Consumer Goods	10.0%	10.0%	7.3%	8.5%	4.0%	9.9%	5.2%	5.6%	6.3%
Industrials	5.7%	10.5%	11.5%	11.2%	18.3%	16.7%	22.1%	29.0%	26.3%
Basic Materials	6.3%	5.6%	10.0%	6.1%	11.5%	12.5%	13.8%	12.1%	17.2%
Healthcare	3.6%	6.7%	1.8%	11.2%	7.1%	7.9%	8.4%	7.1%	5.8%
Utilities	2.6%	3.3%	6.8%	6.8%	4.8%	4.7%	2.3%	1.4%	0.4%
Telecom	1.6%	3.2%	3.1%	0.6%	0.6%	1.8%	1.0%	1.6%	0.6%
Diversified	--	--	--	0.9%	0.4%	0.2%	0.8%	1.4%	1.5%

The table below shows the sector representation in key S&P BSE benchmark indices on March 31, 2019.

Sector	S&P BSE 500	S&P BSE 100	S&P BSE SENSEX
Finance	33.51%	36.11%	43.77%
Consumer Discretionary Goods & Services	12.06%	9.15%	7.42%
Information Technology	10.67%	11.95%	14.08%
Energy	9.77%	11.65%	13.19%
Fast Moving Consumer Goods	9.32%	10.14%	9.55%
Industrials	7.98%	6.20%	5.21%
Basic Materials	7.03%	6.17%	1.89%
Healthcare	5.07%	4.49%	1.32%
Utilities	3.00%	2.62%	2.46%
Telecom	1.41%	1.52%	1.12%
Diversified	0.20%	--	--

Sector representation in each of the above indices has evolved in line with the evolution of the overall market. The dominance of certain sectors over others can be attributed to the size of the companies in these sectors along with the objective of each of these indices.

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For example, the S&P BSE SENSEX is comprised of 30 large, well-established and financially sound Indian companies across key sectors. On March 31, 2019, the largest three sectors in the index were Finance, Information Technology, and Energy. This is in contrast to the market where Consumer Discretionary Goods and Services (“CDGS”) features among the top three. As seen above, since CDGS is smaller than Energy in the Large Cap space, it has a lower representation in the S&P BSE SENSEX.

IMPACT ANALYSIS

In order to provide further information and context on the subject of sector diversification, AIPL has considered three scenarios to assess the impact on index turnover for the S&P BSE 500, S&P BSE 100 and S&P BSE SENSEX.

Scenario	Description
1	Constituents are weighted by float-adjusted market capitalization ("FMC"), subject to a maximum sector weight of 25%.
2	Constituents are weighted by FMC, subject to a maximum sector weight of 35%.
3	Constituents are weighted by FMC, subject to a maximum sector weight being equal to the weight of the largest sector within the S&P BSE AllCap, a broad market index.

For more information on the S&P BSE AllCap, please refer to the *S&P BSE AllCap Methodology*, available [here](#).

The tables below and on the following page show the theoretical one-time turnover for the S&P BSE 500, S&P BSE 100, and S&P BSE SENSEX had the indices been capped at every semi-annual rebalancing as compared to the actual turnover based on the current methodology.

S&P BSE 500								
Rebalancing	Current Methodology	Scenario 1		Scenario 2		Scenario 3		Largest Sector Weight
	Actual Turnover	Theoretical Turnover	Incremental Turnover	Theoretical Turnover	Incremental Turnover	Theoretical Turnover	Incremental Turnover	
Jun 2017	0.43%	5.46%	5.03%	0.43%	0.00%	1.46%	1.03%	29%
Dec 2017	0.53%	5.23%	4.70%	0.53%	0.00%	1.31%	0.79%	29%
Jun 2018	0.97%	6.47%	5.50%	0.97%	0.00%	0.92%	-0.05%	31%
Dec 2018	0.45%	7.49%	7.04%	0.45%	0.00%	0.59%	0.14%	32%

S&P BSE 100								
Rebalancing	Current Methodology	Scenario 1		Scenario 2		Scenario 3		Largest Sector Weight
	Actual Turnover	Theoretical Turnover	Incremental Turnover	Theoretical Turnover	Incremental Turnover	Theoretical Turnover	Incremental Turnover	
Jun 2017	3.77%	9.53%	5.76%	3.77%	0.00%	5.62%	1.85%	29%
Dec 2017	2.21%	8.87%	6.66%	2.21%	0.00%	4.96%	2.76%	29%
Jun 2018	0.69%	8.91%	8.22%	0.69%	0.00%	2.91%	2.22%	31%
Dec 2018	0.37%	9.97%	9.60%	0.37%	0.00%	3.01%	2.64%	32%

S&P BSE SENSEX								
Rebalancing	Current Methodology	Scenario 1		Scenario 2		Scenario 3		Largest Sector Weight
	Actual Turnover	Theoretical Turnover	Incremental Turnover	Theoretical Turnover	Incremental Turnover	Theoretical Turnover	Incremental Turnover	
Jun 2017	4.11%	12.02%	7.91%	3.99%	-0.12%	8.42%	4.31%	29%
Dec 2017	4.37%	16.23%	11.86%	7.32%	2.95%	12.67%	8.30%	29%
Jun 2018	1.40%	16.27%	14.87%	6.27%	4.87%	10.27%	8.87%	31%
Dec 2018	3.24%	19.29%	16.05%	9.69%	6.45%	12.57%	9.33%	32%

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SURVEILLANCE MEASURES

Additionally, S&P BSE index methodologies account for certain BSE exchange surveillance measures in an attempt to enhance the replicability of the indices. The table below summarizes selected surveillance measures that currently form part of the index rules.

Surveillance Measure	Surveillance Objective	Applicable Index Methodology Rule
Graded Surveillance Measure	Additional surveillance of securities that had an abnormal price increase not commensurate with financial health and fundamentals like earnings, book value, fixed assets, net worth, P/E multiple, etc.	<p>Stocks on the Graded Surveillance Measure (“GSM”) list are ineligible for index inclusion.</p> <p>On a monthly basis, companies added to the GSM list are dropped. The effective date of the drop is at the open of the Tuesday following the first Monday of each month. The reference date for the GSM list data is the third Friday of the previous month.</p> <p>Any company dropped due to its inclusion on the GSM list must remain off the GSM list for six consecutive months prior to the rebalancing reference date in order to be reconsidered for index inclusion.</p>
Surveillance Objected Stocks	Internal review by BSE’s surveillance team to flag stocks that should not be included in any S&P BSE index.	<p>Stocks subject to surveillance objections are ineligible for inclusion in any S&P BSE index.</p> <p>At each quarterly rebalancing, any stock flagged as “Surveillance Objected” is dropped from the indices and is considered ineligible for index addition.</p>

QUESTIONS

Please answer the following questions and provide AIPL with the reasoning behind your answers:

- 1. Do you have any concerns or comments with regard to sector diversification and representation in benchmark indices?**
- 2. If you answered Yes to Question 1, what are your concerns or comments?**
- 3. Do you believe there is a limit to the representation that a single industry, sector, or stock should be allowed to reach in a broad benchmark or bell-weather index?**
- 4. If you answered Yes to Question 3, what do you believe the appropriate limit should be?**
- 5. Do you believe the current methodologies sufficiently account for exchange surveillance measures?**
- 6. If you answered No to Question 5, what other exchange surveillance measures do you believe could be incorporated into S&P BSE index methodologies?**

Your participation in this consultation is important as we gather information from various market participants in order to properly evaluate your views and preferences. AIPL will make responses to consultations freely available upon request.³ If you do not want your response to be made available, you must clearly state that in your response. Please respond to this survey by **June 21, 2019**. After this date, AIPL will no longer accept survey responses. Prior to the Index Committee’s final review, AIPL will consider the issues and may request clarifications from respondents as part of that review. Alternative

³ Individual and company names as well as contact details will be redacted.

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options to the proposed questions after the deadline require that the consultation be re-opened to the public.

To participate in this consultation, please visit the online survey available [here](#).

For further information about this consultation, please contact AIPL at index_services@spglobal.com.

Please be advised that all comments from this consultation will be reviewed and considered before a final decision is made; however, AIPL makes no guarantees or is under any obligation to comply with any of the responses. The survey may result in no changes or outcome of any kind. If AIPL decides to change the index methodology, an announcement will be posted on our website.

Thank you for taking the time to complete this survey.

For more information about S&P BSE Indices, please visit www.asiaindex.co.in.

About ASIA INDEX PRIVATE LIMITED

Asia Index Pvt. Ltd is a 50-50 partnership between S&P Dow Jones Indices LLC, the world's largest provider of financial market indices, and BSE Ltd, Asia's oldest stock exchange and home to the iconic SENSEX index – a leading indicator of Indian equity market performance. Asia Index Pvt. Ltd, which combines the benchmarks, market intelligence, and insights of both parent companies, each established more than 115 years ago, aims to provide a full array of indices enabling global and domestic investors to participate in South Asia's vibrant economies. The Company is best known for calculating, publishing, and maintaining a diverse family of Asian indices under the umbrella brand, S&P BSE Indices.

About BSE Ltd

BSE (formerly Bombay Stock Exchange) established in 1875, is Asia's first & now the world's fastest Stock Exchange with a speed of 6 microseconds. BSE is India's leading exchange group and has played a prominent role in developing the Indian capital market. BSE is a corporatized and demutualised entity, with a broad shareholder base that includes the leading global exchange- Deutsche Bourse, as a strategic partner. BSE provides an efficient and transparent market for trading in equity, debt instruments, equity derivatives, currency derivatives, interest rate derivatives, mutual funds and stock lending and borrowing. BSE also has a dedicated platform for trading in equities of small and medium enterprises (SMEs) that has been highly successful. BSE provides a host of other services to capital market participants including risk management, clearing, settlement, market data services and education. It has a global reach with customers around the world and a nation-wide presence. BSE's systems and processes are designed to safeguard market integrity, drive the growth of the Indian capital market and stimulate innovation and competition across all market segments. Indian Clearing Corporation Limited, a wholly owned subsidiary of BSE, acts as the central counterparty to all trades executed on the BSE trading platform and provides full novation, guaranteeing the settlement of all bonafide trades executed. BSE Institute Ltd, another fully owned subsidiary of BSE runs one of the most respected capital market educational institutes in the country. Central Depository Services Ltd. (CDSL), a subsidiary of BSE, is one of the two Depositories in India.

About S&P DOW JONES INDICES

S&P Dow Jones Indices is the largest global resource for essential index-based concepts, data and research, and home to iconic financial market indicators, such as the S&P 500® and the Dow Jones Industrial Average®. More assets are invested in products based on our indices than products based on indices from any other provider in the world. Since Charles Dow invented the first index in 1884, S&P DJI has been innovating and developing indices across the spectrum of asset classes helping to define the way investors measure and trade the markets.

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FOR MORE INFORMATION:

Asia Index Private Limited
index_services@spglobal.com