

Market Consultation

To: Market Participants
From: Indices Department
Date: 15 October 2013
Subject: **Market Consultation: Proposed Resources Reclassification**

1. Executive Summary

FTSE/JSE has received requests from some market participants to expand the definition of the SA Resource sector. Under this proposal, there are companies currently defined as SA Industrials which would be reclassified as SA Resources. The current SA Resource sector incorporates companies classified in the Industry Classification Benchmark (ICB) sectors Oil & Gas Producers (0530) or Mining (1770). The proposal is to extend this to include two complete ICB Industries, namely Oil & Gas and Basic Materials. As a result, the expanded SA Resources sector would include companies classified as Chemicals, Forestry & Paper, and Industrial Metals and Mining.

FTSE/JSE requests comment from market participants that are currently using the Resource / Industrial / Financial SA Sector classification applied in the FTSE/JSE indices in order to assess the impact and viability of this proposal.

2. ICB Classification

The SA sector classification into SA Resources, SA Industrials or SA Financials is based on the global ICB methodology (<http://www.icbenchmark.com/>). ICB is used to categorise all companies listed on the JSE, regardless of their eligibility for the FTSE/JSE Africa Index Series. Each company is allocated to one of 114 subsectors according to the nature of its business, measured by revenue. Each subsector rolls up into one of 41 sectors, which themselves roll up into 19 supersectors. At the top level of the hierarchy are 10 industries. The current ICB structure is provided in full in Appendix A.

3. Current SA Sector Classification

Prior to the launch of the FTSE/JSE Africa Index Series in 2002, all JSE companies were classified by SA Sector as SA Resources, SA Financials or SA Industrials. The introduction of FTSE/JSE indices also brought a new classification system used for indices, namely the Global Classification System (GCS). At that point, a straightforward process was done in order to map the GCS classification to the original SA Sector classification, and the two systems were run in parallel. Similarly, when ICB replaced GCS from 2007, SA Sector was redefined in terms of the ICB sectors and industries.



Company classification is currently done at an ICB level, and a mapping table is used to determine the SA Sector from the ICB classification as follows:

- SA Resources ICB Sectors Oil & Gas Producers (0530) and Mining (1770)
- SA Financials ICB Industry Financials (8000)
- SA Industrials All remaining companies

4. SA Sector Indices

There are currently a number of FTSE/JSE indices that are based on the SA Sector classification, and would be impacted by a change to the sector definition. Three broadly representative indices divide the FTSE/JSE All Share Index by SA Sector (i.e. SA Resources, Financials, SA Industrials), while three replicable indices capture the most liquid, tradable instruments in each sector (i.e. RESI 10, FINI 15, INDI 25). In addition, there are two variants that capture the combined set of SA Financials and SA Industrials (i.e. J213 and J250).

Based on the free float adjusted market cap calculation used in the indices, SA Resources currently account for around 26% of the All Share, SA Industrials for 55% and SA Financials for 19%. The three tradable indices RESI 10, FINI 15 and INDI 25 capture just over 88% of this universe.

5. Expanded SA Sector Classification

Some market participants feel that there are currently companies classified as SA Industrial which are commonly considered to be SA Resource companies. A proposed solution to align the SA Sector definition with this view is to expand the SA Resource definition to an ICB industry level rather than an ICB sector level.

Table 1 presents the methodology change. The current definition of sectors 0530 and 1770 is highlighted in red, while the expanded definition of 0001 and 1000 is highlighted in blue:

Industry	Supersector	Sector	Subsector
0001 Oil & Gas	0500 Oil & Gas	0530 Oil & Gas Producers	0533 Exploration & Production
			0537 Integrated Oil & Gas
		0570 Oil Equipment, Services & Distribution	0573 Oil Equipment & Services
			0577 Pipelines
		0580 Alternative Energy	0583 Renewable Energy Equipment
		0587 Alternative Fuels	
1000 Basic Materials	1300 Chemicals	1350 Chemicals	1353 Commodity Chemicals
			1357 Specialty Chemicals
	1700 Basic Resources	1730 Forestry & Paper	1733 Forestry
			1737 Paper
		1750 Industrial Metals & Mining	1753 Aluminium
			1755 Nonferrous Metals
			1757 Iron & Steel
		1770 Mining	1771 Coal
			1773 Diamonds & Gemstones
			1775 General Mining
1777 Gold Mining			
		1779 Platinum & Precious Metals	

Table 1: Current & Proposed SA Resources

This would in effect increase the size of the SA Resource sector from its current inclusion of two ICB Sectors to an expanded seven. Note however that there are currently no JSE-listed instruments in the 0570 and 0580 ICB sectors, so the immediate impact would be to reclassify chemical, forestry, and industrial metals and mining companies as Resources.

A list of all companies in the All Share Index that are impacted by this change is provided in Table 2. There are 10 companies in total, with a combined weight in the All Share Index of around 2.75%.

Alpha	Instrument	ICB Subsector	All Share Weight
MNP	Mondi Plc	Paper	1.07%
MND	Mondi Ltd	Paper	0.34%
KIO	Kumba Iron Ore	Iron & Steel	0.48%
AFE	AECI	Speciality Chemicals	0.24%
SAP	Sappi	Paper	0.23%
OMN	Omnia Holdings Ltd	Speciality Chemicals	0.21%
ACL	ArcelorMittal South Africa Ltd	Iron & Steel	0.10%
AFX	African Oxygen	Speciality Chemicals	0.05%
PAM	Palabora Mining	General Mining	0.03%
YRK	York Timber Holdings	Forestry	0.01%

Table 2: All Share Constituents impacted by expanded definition of Resources

6. Impact of the Expanded Classification on Index Weights

Using index weights from 30 September 2013, the expanded SA Resource definition would impact 10 companies in the FTSE/JSE All Share Index, increasing the weight of SA Resources from 26% to 29%:

	ICB Sector							Total
	0530	0570	0580	1350	1730	1750	1770	
Current No. of Constituents	1						20	21
Current Weight	4.56%						21.88%	26.44%
Proposed No. of Constituents	1			3	4	3	20	31
Proposed Weight	4.56%			0.50%	1.65%	0.60%	21.88%	29.19%

Table 3: Constituent Changes and Weight in All Share

There would also be an impact on the RESI 10 tradable index, with Kumba Iron Ore and Mondi potentially being added to the index. Currently, the two lowest ranking constituents in this index are Gold Fields and African Rainbow Minerals. The RESI 10 selects the ten largest SA Resource companies in the All Share Index, based on gross market capitalisation.

There will also be a weighting shift in the Top 40 indices as some companies move from SA Industrials to SA Resources. Table 3 gives an indication of the SA Sector weights in the Top 40 and SWIX 40 indices using the current definition and the expanded definition:

SA Sector	Top 40		SWIX 40	
	Current	Expanded	Current	Expanded
Financials	16.0%	16.0%	20.4%	20.4%
Industrials	54.3%	52.0%	56.8%	54.6%
Resources	29.7%	31.9%	22.7%	25.0%

Table 3: Impact of expanded Resources definition on Top 40 and SWIX 40

7. Responding to the consultation

FTSE/JSE is aware of the large number of market participants that are currently using the indices for various purposes. The expansion of the SA Resource definition to include five additional ICB sectors could thus impact various index users in different ways.

All interested parties are thus invited to comment on this proposal so that FTSE/JSE can take the correct decision for the South African market. Market Participants are requested to comment on:

- Would the expanded definition of SA Resources be better aligned with market convention?
- If not, what definition of SA Resources would be most appropriate?
- Are there any concerns around the practical implementation of this proposal?

Please submit feedback by email, on or before Friday, 15 November 2013 to indices@jse.co.za.

All feedback will be discussed at the December 2013 AC Meeting in order to assess the impact and viability of the proposal. Please contact Mark Randall on 011 520 7137 for further details.

Appendix A – Complete ICB Structure

Industry	Supersector	Sector	Subsector
0001 Oil & Gas	0500 Oil & Gas	0530 Oil & Gas Producers	0533 Exploration & Production
			0537 Integrated Oil & Gas
		0570 Oil Equipment, Services & Distribution	0573 Oil Equipment & Services
			0577 Pipelines
		0580 Alternative Energy	0583 Renewable Energy Equipment
0587 Alternative Fuels			
1000 Basic Materials	1300 Chemicals	1350 Chemicals	1353 Commodity Chemicals
			1357 Specialty Chemicals
	1700 Basic Resources	1730 Forestry & Paper	1733 Forestry
			1737 Paper
		1750 Industrial Metals & Mining	1753 Aluminum
			1755 Nonferrous Metals
	1770 Mining	1757 Iron & Steel	
		1771 Coal	
		1773 Diamonds & Gemstones	
		1775 General Mining	
		1777 Gold Mining	
1779 Platinum & Precious Metals			
2000 Industrials	2300 Construction & Materials	2350 Construction & Materials	2353 Building Materials & Fixtures
			2357 Heavy Construction
	2700 Industrial Goods & Services	2710 Aerospace & Defense	2713 Aerospace
			2717 Defense
		2720 General Industrials	2723 Containers & Packaging
		2727 Diversified Industrials	
		2730 Electronic & Electrical Equipment	2733 Electrical Components & Equipment
			2737 Electronic Equipment
		2750 Industrial Engineering	2753 Commercial Vehicles & Trucks
		2757 Industrial Machinery	
	2770 Industrial Transportation	2771 Delivery Services	
		2773 Marine Transportation	
		2775 Railroads	
		2777 Transportation Services	
	2779 Trucking		
	2790 Support Services	2791 Business Support Services	
		2793 Business Training & Employment Agencies	
		2795 Financial Administration	
2797 Industrial Suppliers			
2799 Waste & Disposal Services			
3000 Consumer Goods	3300 Automobiles & Parts	3350 Automobiles & Parts	3353 Automobiles
			3355 Auto Parts
			3357 Tires
	3500 Food & Beverage	3530 Beverages	3533 Brewers
			3535 Distillers & Vintners
		3537 Soft Drinks	
		3570 Food Producers	3573 Farming, Fishing & Plantations
	3577 Food Products		
	3700 Personal & Household Goods	3720 Household Goods & Home Construction	3722 Durable Household Products
			3724 Nondurable Household Products
			3726 Furnishings
			3728 Home Construction
		3740 Leisure Goods	3743 Consumer Electronics
			3745 Recreational Products
		3760 Personal Goods	3747 Toys
			3763 Clothing & Accessories
	3765 Footwear		
	3767 Personal Products		
3780 Tobacco	3785 Tobacco		

Industry	Supersector	Sector	Subsector	
4000 Health Care	4500 Health Care	4530 Health Care Equipment & Services	4533 Health Care Providers	
			4535 Medical Equipment	
			4537 Medical Supplies	
		4570 Pharmaceuticals & Biotechnology	4573 Biotechnology	
			4577 Pharmaceuticals	
5000 Consumer Services	5300 Retail	5330 Food & Drug Retailers	5333 Drug Retailers	
			5337 Food Retailers & Wholesalers	
			5371 Apparel Retailers	
		5370 General Retailers	5373 Broadline Retailers	
			5375 Home Improvement Retailers	
			5377 Specialized Consumer Services	
			5379 Specialty Retailers	
	5500 Media	5550 Media	5553 Broadcasting & Entertainment	
			5555 Media Agencies	
			5557 Publishing	
	5700 Travel & Leisure	5750 Travel & Leisure	5751 Airlines	
			5752 Gambling	
			5753 Hotels	
			5755 Recreational Services	
			5757 Restaurants & Bars	
5759 Travel & Tourism				
6000 Telecommunications	6500 Telecommunications	6530 Fixed Line Telecommunications	6535 Fixed Line Telecommunications	
		6570 Mobile Telecommunications	6575 Mobile Telecommunications	
7000 Utilities	7500 Utilities	7530 Electricity	7535 Conventional Electricity	
			7537 Alternative Electricity	
		7570 Gas, Water & Multiutilities	7573 Gas Distribution	
			7575 Multiutilities	
			7577 Water	
8000 Financials	8300 Banks	8350 Banks	8355 Banks	
			8500 Insurance	8530 Nonlife Insurance
	8534 Insurance Brokers			
	8536 Property & Casualty Insurance			
	8538 Reinsurance			
	8600 Real Estate	8630 Real Estate Investment & Services	8570 Life Insurance	8575 Life Insurance
				8670 Real Estate Investment Trusts
			8637 Real Estate Services	
			8671 Industrial & Office REITs	
			8672 Retail REITs	
			8673 Residential REITs	
			8674 Diversified REITs	
			8675 Specialty REITs	
	8676 Mortgage REITs			
	8677 Hotel & Lodging REITs			
	8700 Financial Services	8770 Financial Services	8771 Asset Managers	
			8773 Consumer Finance	
			8775 Specialty Finance	
			8777 Investment Services	
8779 Mortgage Finance				
8980 Equity Investment Instruments			8985 Equity Investment Instruments	
8990 Nonequity Investment Instruments	8995 Nonequity Investment Instruments			
9000 Technology	9500 Technology	9530 Software & Computer Services	9533 Computer Services	
			9535 Internet	
			9537 Software	
			9570 Technology Hardware & Equipment	9572 Computer Hardware
		9574 Electronic Office Equipment		
		9576 Semiconductors		
		9578 Telecommunications Equipment		