

Market Consultation

To: Market Participants
From: Indices Department
Date: 6 July 2021
Subject: Request for Comment: Naspers/Prosus Capping **Updated**

UPDATED: Due to requests from market participants for an extension to the market consultation period, the market consultation closing date will be extended from Tuesday, 13 July 2021 to Tuesday, 20 July 2021. No further changes have been made to the market consultation.

1. Introduction

Following the September 2019 FTSE/JSE Index Series implementation of the Naspers capitalisation issue a [market consultation](#) was published to gain insights on how to address the resultant combined weight of Naspers and Prosus in the FTSE/JSE Capped indices, specifically the Capped SWIX All Share Index (J433). Following the feedback received from this market consultation FTSE/JSE [announced](#) that the proposed amendment to the capping rules would not be implemented at that stage. Further to that announcement, some market participants have challenged the validity of the process that was followed in coming to this decision, and other participants and industry bodies have submitted new motivation to FTSE/JSE to review the decision.

As such, FTSE/JSE is requesting comment from index users on whether the current capping methodology requires amendment. In particular, index users have suggested that the FTSE/JSE Capped SWIX All Share Index, as the *de facto* benchmark for local active South African equity managers, is no longer optimal for its intended purpose, and could be considered for a targeted rules enhancement.

2. Proposed Capping Amendment

Capping is applied in certain FTSE/JSE indices to reduce single stock exposure. Since Naspers and Prosus are two separate companies, the capping is currently applied separately, and as such the combined index weight of the two companies can be as much as 20% in a 10% capped index. However, Naspers derives a dominant portion of its value from its underlying holding in Prosus, and many index users believe that the principle of the capping approach should result in the combined group weight being restricted to 10% in the capped indices.

The 2019 proposal document suggested that two separate companies in a capped index that had a group structure relationship should be jointly capped if the valuation of the parent/holding company was dominated by the valuation of its stake in the second company. The proposed wording of the rule is as follows:

To meet the requirements for capping two entities together, on review cut date:

- Both the parent company and subsidiary company have to be JSE listed
- The parent company shareholding in the subsidiary company is restricted for free float purposes (cross-holding)
- Consider the gross market cap of the holding company and the percentage of the subsidiary gross market cap held by the parent company
- If this holding is 75% or higher, the two companies will be considered as a single entity for capping purposes in all capped indices where they are both constituents
- If this holding falls to 65% or below at a subsequent quarterly review, the two entities will no longer be capped as one entity

The following example was provided:

Example:

- Gross market cap of holding company – Rb954
- Gross market cap of subsidiary company – Rb1,707
- Restricted holding of parent company in subsidiary – 74% (Rb1,264)

$$x = \frac{\text{Rb1,707} \times 74\%}{\text{Rb954}} = 132\% > 75\%$$

Two important supporting notes to this proposal are:

- Both companies must be JSE listed and All Share constituents
- The valuation of the parent company market capitalisation and its stake in the subsidiary will be based on public JSE closing prices

The general principle in this instance would be to consider a holding company whose valuation is almost exclusively dominated by its holding in a listed subsidiary. Where an index constituent has a controlling stake in another index constituent, and the market value of that stake is greater than 75% of the prevailing market capitalisation of the subsidiary company, then the two companies shall be considered at a combined group valuation level for index capping purposes only.

3. Information Required

In order to effectively understand the context of each respondent, and to more effectively analyse contrasting views to this request for comment, please provide the following supporting information with your response:

- 3.1 Name of company.
- 3.2 Name, surname and designation of respondent.
- 3.3 Do you currently subscribe to receive FTSE/JSE Capped SWIX All Share (J433) and FTSE/JSE Capped SWIX Top 40 (J430) index data? Alternatively, do you have an active tracking license, structured product license or multi-use license for one of these indices?
- 3.4 Please briefly describe how you currently utilise the Capped SWIX indices data, both All Share and Top 40 variants.
- 3.5 What is your company's current Assets Under Management or Assets Under Advisement that are benchmarked against the FTSE/JSE Capped SWIX All Share index? Ideally, please provide a split of institutional vs. unit trust.
- 3.6 What is your company's current passive tracking AUM against the FTSE/JSE Capped SWIX All Share or Top 40 index?
- 3.7 Does your company utilise the FTSE/JSE Capped SWIX All Share index in any other manner, e.g., employee scheme, OTC derivative or other instrument?

4. Feedback Required

Following the 2019 consultation and various bilateral discussions, FTSE/JSE believes that many of the arguments in support and against the proposal have been well understood. Respondents that have previously provided qualitative support for their views are not required to provide the same information again in response to this consultation. We would nonetheless invite any qualitative submissions or comments from respondents in support of their views.

When responding to this consultation, please provide feedback to the questions listed below. For the purposes of the questions below, the term “Group Entity Capping” refers to the proposed capping amendment detailed in paragraph 2 above.

- 4.1 Do you believe that Group Entity Capping should be applied in the FTSE/JSE Capped SWIX indices (J433 and J430)?
- 4.2 Do you believe that Group Entity Capping should be applied in **all** FTSE/JSE Capped indices?
- 4.3 If Group Entity Capping is not applied, should the standard capping level of 10% in FTSE/JSE indices be reduced to a lower level? If so, what is the appropriate capping level?

5. Responding to the Consultation

It is important to FTSE/JSE to be aware of the impact to clients as well as any unintended consequences of the weighting concentration of Naspers and Prosus in the FTSE/JSE Index Series. FTSE/JSE is committed to providing market benchmarks that are credible and consistent, and the purpose of this market consultation is to obtain feedback from index users regarding their concerns around the proposed solution.

Please provide us with your response to the questions in the consultation, as well as any additional supporting information, by **Tuesday, 20 ~~13~~ July 2021** at the following email address: indices@jse.co.za

When determining the timeline for the implementation of any decision, FTSE/JSE is mindful of the broad usage of these indices in the market and the need to provide appropriate notice. This document is not confidential and should be distributed as widely as possible to all stakeholders.