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# FTSE Country Classification – March 2018 Interim Update

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## 1. Classification of Markets

A formal interim review of country classification within the FTSE global equity indexes is conducted every March using a comprehensive, transparent and consistent methodology to keep investors fully informed on the markets which had been placed on the Watch List the previous September.

## 2. FTSE Watch List

In order to ensure that potential movement of markets between classifications is completely transparent to investors, a Watch List of markets being considered for reclassification is maintained.

The following markets were placed on the Watch List following the Annual Review in September 2017:

- **China A-share:** possible inclusion as Secondary Emerging
- **Iceland:** possible inclusion as Frontier
- **Romania:** possible reclassification from Frontier to Secondary Emerging
- **Saudi Arabia:** possible inclusion as Secondary Emerging.

## 3. Progress of Watch List markets since September 2017

### Secondary Emerging Watch List

#### Saudi Arabia

FTSE Russell is pleased to announce that Saudi Arabia will be assigned Secondary Emerging market status within the FTSE Country Classification scheme commencing in conjunction with the FTSE Global Equity Index Series (GEIS) semi annual review in March 2019. The details of the implementation of this change will be set out in a separate release by FTSE Russell.

Saudi Arabia was added to the Watch List in September 2015 following the introduction of a Qualified Foreign Investor (QFI) scheme.

During 2017-2018, the Capital Market Authority of Saudi Arabia and the Saudi Arabia Stock Exchange (Tadawul) introduced a number of improvements to the market infrastructure aimed at opening up the domestic market to international investors. These included, but were not limited to the simplification of the QFI registration process and enhancements to the Independent Custody Model (ICM), which included the introduction of a T+2 settlement cycle with a Delivery versus Payment (DvP) model in April 2017.

Consequently, the FTSE Russell Country Classification Advisory Committee has endorsed the following criteria rating changes within the Quality of Markets matrix:

- “No or simple registration process for foreign investors”: upgraded from ‘Not Met’ to ‘Pass’;
- “Settlement – rare incidences of failed trades”: upgraded from ‘Restricted’ to ‘Pass’; and
- “Clearing & Settlement – T+2/T+3”: upgraded from ‘Restricted’ to ‘Pass’.

#### Implementation

Saudi Arabia is projected to have an index weight within FTSE GEIS of 0.25% and 2.7% within the FTSE Emerging Index. Due to this projected size in the Emerging index, FTSE Russell proposes to implement the inclusion of Saudi Arabia in several tranches to ensure mechanisms are operating as expected, thereby minimizing price pressure on new constituents and to spread outflows from those markets being sold down.

The implementation of Saudi Arabia into FTSE GEIS will commence in conjunction with the March 2019 semi-annual review and being completed by December 2019. The initial 25% tranche will be split over March and April 2019 to ensure a smooth phasing in of Saudi Arabia. The remaining 75% will be implemented in conjunction with the quarterly reviews in June, September and December 2019.

	Tranche One	Tranche Two	Tranche Three	Tranche Four	Tranche Five
Review Schedule	March	April	June	September	December
Effective Date	Open Monday 18 March 2019	Open Monday 22 April 2019	Open Monday 24 June 2019	Open Monday 23 September 2019	Open Monday 23 December 2019
Saudi Arabia Inclusion Factor	10%	15%	25%	25%	25%
Total	10%	25%	50%	75%	100%

Full details on the implementation schedule can be found at <http://www.ftse.com/products/indices/country-classification>

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## Saudi Aramco

FTSE methodology states that initial public offering (IPOs) which meet fast entry thresholds are added to FTSE GEIS after the close of business on the fifth day of trading.

Although the details regarding the proposed IPO of Aramco have yet to be confirmed, consensus valuations range from US\$ 1-2trn. Assuming a mid-range value of US\$ 1.5trn and an initial public float of 5%, this results in an investable market capitalisation of USD 75bn which would be equivalent to an approximate projected index weight of 1.35% within the FTSE Emerging All Cap (with Saudi Arabia already transitioned into FTSE GEIS).

There are three potential scenarios regarding the timing of the Aramco IPO:

- If the IPO of Aramco takes place **prior** to the commencement of Saudi Arabia's implementation into FTSE GEIS (March 2019), Aramco would be included as part of the Saudi Arabia implementation.
- If the IPO of Aramco takes place **during** the transition process, i.e. between March and December 2019, the proportion of Saudi Aramco to be included at IPO would be equal to the percentage of Saudi Arabia that had been transitioned as of the IPO date. The remainder would be added in conjunction with the remaining transition of Saudi Arabia.
- If the IPO of Aramco takes place **after** the transition of Saudi Arabia has been completed (after December 2019), **Aramco would be treated as a standard IPO.**

FTSE Russell will provide additional details as and when the IPO of Saudi Aramco has been announced to the market.

## China A-share market

Since the addition of China A-shares to the FTSE Watch List, FTSE Russell has evaluated the market based on the combined experience of the Qualified Foreign Institutional Investor (QFII) and Renminbi Qualified Foreign Institutional Investor (RQFII) routes. As a result of recent enhancements to Stock Connect, separate evaluations for the China A-share market against the three access routes available to foreign investors have been conducted to determine the extent to which the three access routes meet the requirements for Secondary Emerging.

The following table illustrates the rating changes against the FTSE Quality of Markets matrix criteria resulting from the evaluation of the individual routes in March 2018:

FTSE Quality of Markets	Secondary Emerging	QFII	RQFII	Stock Connect
No objection to or significant restrictions or penalties applied to the investment of capital or the repatriation of capital and income	X	Retain as Not Met	Retain as Not Met	Upgrade from Not Met to Restricted
Free and well developed foreign exchange market		Retain as Not Met	Retain as Not Met	Upgrade from Not Met to Restricted
No or simple registration process		Retain as Not Met	Retain as Not Met	Upgrade from Not Met to Pass
Clearing & Settlement – T+2 / T+3	X	Retain as Not Met (T+0)	Retain as Not Met (T+0)	Upgrade from Not Met to Restricted (T+0/T+1)
Custody – Omnibus and Segregated account facilities available to international investors		Downgrade from Pass to Restricted	Downgrade from Pass to Restricted	Downgrade from Pass to Restricted
Brokerage – sufficient competition to ensure high quality broker services	X	Downgrade from Pass to Restricted	Downgrade from Pass to Restricted	Retain as Pass
Stock lending is permitted		Retain as Not Met	Retain as Not Met	Upgrade from Not Met to Restricted
Short selling is permitted		Retain as Not Met	Retain as Not Met	Upgrade from Not Met to Restricted
Efficient Trading Mechanism		Downgrade from Pass to Restricted	Downgrade from Pass to Restricted	Downgrade from Pass to Restricted

The following table illustrates how the three separate routes are rated against the nine criteria required for Secondary Emerging:

FTSE Quality of Markets	Secondary Emerging	QFII	RQFII	Stock Connect
Formal stock market regulatory authorities actively monitor market	X	Pass	Pass	Pass
No objection to or significant restrictions or penalties applied to the investment of capital or the repatriation of capital and income	X	Not Met	Not Met	Restricted
Settlement – rare incidence of failed trades	X	Pass	Pass	Pass
Custody – Sufficient competition to ensure high quality custodian services	X	Pass	Pass	Pass
Clearing & Settlement – T+2/T+3	X	T+0	T+0	T+0/T+1
Brokerage – sufficient competition to ensure high quality broker services	X	Restricted	Restricted	Pass
Liquidity – sufficient broad market liquidity to support sizeable global investment	X	Pass	Pass	Pass
Transaction costs – implicit and explicit costs to be reasonable and competitive	X	Pass	Pass	Pass
Transparency – market depth information / visibility and timely trade reporting process	X	Pass	Pass	Pass

The QFII and RQFII schemes continue to possess certain limitations including (but not limited to):

- Capital controls: the initial principle has to be locked-up for a minimum of three months under QFII and for non open-ended funds under RQFII; additionally there are monthly restrictions on repatriation levels under QFII; and
- T+0 settlement cycle: accessing China A-shares via the QFII/RQFII routes requires trades to be pre-funded.

There are no capital controls under Stock Connect. However, a daily quota limit exists. Once the quota is reached, Stock Connect is suspended for the day. Without a change to the daily limits, there is a possibility that the quota could be breached at a global benchmark rebalance.

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In addition, stock suspensions continue to prove problematic to institutional investors. On average approximately 8% of China A-share securities in the FTSE China A All Cap Index are currently suspended; this equates to approximately 5% of the investable capitalisation of the index. The suspensions can be for extended periods.

The China A-share market is retained on the Watch List, and will be reviewed for possible inclusion as a Secondary Emerging market within the FTSE Country Classification scheme at the Annual Review in September 2018. FTSE Russell acknowledges the efforts of the Chinese authorities to increase the accessibility of the China A-share market for international investors and will continue to work closely with the Chinese authorities towards the inclusion of China A-shares in FTSE GEIS.

FTSE Global China A Inclusion Indexes are available for market participants, with a choice of how to include China A-shares in global benchmarks. The series also includes FTSE China A Indexes and China A Stock Connect Indexes.

## **Romania**

Romania was added to the Watch List in September 2016 for possible reclassification to Secondary Emerging market status.

The single outstanding criterion is “Liquidity – Sufficient broad market liquidity to support sizeable global investment”, which is currently rated as ‘Not Met’. FTSE Russell acknowledges the efforts of the Bucharest Stock Exchange to bring IPOs to the market and to improve liquidity levels on the exchange.

Romania is retained on the Watch List as a Frontier market, and will be reviewed for possible reclassification as a Secondary Emerging market, within the FTSE Country Classification scheme at the Annual Review in September 2018.

## **Frontier Watch List**

### **Iceland**

Iceland was added to the Watch List in September 2017 for possible inclusion as a Frontier market, following the removal of the capital controls on new investment in Icelandic equities which had been in place since the Icelandic banking crisis in 2008/2009.

Iceland currently meets the five FTSE Quality of Markets criteria required for Frontier market status within the FTSE Country Classification scheme. However, markets must remain on the Watch List for a minimum of one year for evaluation purposes before a reclassification is announced. Hence Iceland will be retained on the Watch List and be reviewed for possible classification as a Frontier market at the Annual Review in September 2018.

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## 4. As part of the September 2017 Annual Review, FTSE announced the following reclassifications:

- **Poland** from Advanced Emerging to Developed market status, effective in conjunction with the GEIS semi annual review in September 2018.
- **Kuwait** from Unclassified to Secondary Emerging market status, effective in two 50% tranches in conjunction with the FTSE GEIS semi annual review in September 2018 and the quarterly review in December 2018.

FAQs supporting these market transitions are available at <http://www.ftse.com/products/indices/country-classification>

## 5. Summary of changes to the September 2017 Watch List markets:

- **Saudi Arabia:** reclassification from Unclassified to Secondary Emerging, commencing from March 2019.

## 6. The March 2018 Watch List is as follows:

- **China A-share:** possible inclusion as Secondary Emerging
- **Iceland:** possible inclusion as Frontier
- **Romania:** possible reclassification from Frontier to Secondary Emerging

For more information please visit: <http://www.ftse.com/products/indices/country-classification>

The table below shows the FTSE classification of markets as at March 2018.

Developed	Advanced Emerging	Secondary Emerging	Frontier
Australia	Brazil	Chile	Argentina
Austria	Czech Republic	China	Bahrain
Belgium/Luxembourg	Greece	Colombia	Bangladesh
Canada	Hungary	Egypt	Botswana
Denmark	Malaysia	India	Bulgaria
Finland	Mexico	Indonesia	Côte d'Ivoire
France	Poland*	Pakistan	Croatia
Germany	South Africa	Peru	Cyprus
Hong Kong	Taiwan	Philippines	Estonia
Ireland	Thailand	Qatar	Ghana
Israel	Turkey	Russia	Jordan
Italy		UAE	Kazakhstan
Japan			Kenya
Netherlands		Kuwait**	Latvia
New Zealand		Saudi Arabia ***	Lithuania
Norway			Macedonia
Portugal			Malta
Singapore			Mauritius
South Korea			Morocco
Spain			Nigeria
Sweden			Oman
Switzerland			Palestine
UK			Romania
USA			Serbia
			Slovakia
			Slovenia
			Sri Lanka
			Tunisia
			Vietnam

\*Poland to be promoted to Developed market status, effective from September 2018.

\*\*Kuwait to be promoted to Secondary Emerging market status, commencing from September 2018.

\*\*\*Saudi Arabia to be promoted to Secondary Emerging market status, commencing from March 2019.

Source: FTSE Russell as at March 2018. Past performance is no guarantee of future results. Please see disclaimer for important legal information.

# Matrix of markets

	SEGMENTS	AMERICAS	ASIA PACIFIC	EUROPE	MEA
	All-World World Development Advanced Emerging Emerging Secondary Emerging EMEA All-World BRIC All-World ex USA All-World ex NA Developed ex USA Developed ex NA All-World Americas All-World North America All-World Latin America Emerging Latin America World ex Japan All-World ex Asia Developed ex Japan (FTSE Kaigan) Developed Asia Pacific Developed Asia Pacific ex Japan Developed Europe Asia Pacific All-World Europe-Asia Pacific All-World Asia Pacific All-World Asia Pacific ex Japan All-World Asia Pacific ex Japan, India & Pakistan All-World Asia Pacific ex Japan, Australia & New Zealand All-World Asia Pacific ex Japan, Hong Kong, Australia & New Zealand All-World Asia Pacific ex Japan, Australia, N.Zealand, India & Pakistan All-World Asean All-World Greater China Emerging Asia Pacific All-World ex UK All-World ex Eurozone Developed ex Eurozone Developed ex UK Developed Europe Developed Europe ex UK Developed Europe ex Eurozone ex UK All-World Europe All-World Eurozone All-World Europe ex UK All-World Europe ex Eurozone All-World Eastern Europe All-World Nordic Emerging Europe All-World ex South Africa All-World Middle East and Africa				
Australia	•••	••••	••••••••	••••	•
Austria	•••	••••	••••	••••••	•
Belgium/Luxembourg	•••	••••	••••	••••••	•
Brazil	•••	••••	••••	••••	•
Canada	•••	••••	••••	••••	•
Chile	•••	••••	••••	••••	•
China	•••	••••	••••	••••	•
Colombia	•••	••••	••••	••••	•
Czech Republic	•••	••••	••••	••••••	•
Denmark	•••	••••	••••	••••••	•
Egypt	•••	••••	••••	••••	••
Finland	•••	••••	••••	••••••	•
France	•••	••••	••••	••••••	•
Germany	•••	••••	••••	••••••	•
Greece	•••	••••	••••	••••	••
Hong Kong	•••	••••	••••	••••	•
Hungary	•••	••••	••••	••••	•
India	•••	••••	••••	••••	•
Indonesia	•••	••••	••••	••••	•
Ireland	•••	••••	••••	••••••	•
Israel	•••	••••	••••	••••	••
Italy	•••	••••	••••	••••••	•
Japan	•••	••••	••••	••••	•
Korea	•••	••••	••••	••••	•
Malaysia	•••	••••	••••	••••	•
Mexico	•••	••••	••••	••••	•
Netherlands	•••	••••	••••	••••••	•
New Zealand	•••	••••	••••	••••	•
Norway	•••	••••	••••	••••••	•
Pakistan	•••	••••	••••	••••	•
Peru	•••	••••	••••	••••	•
Philippines	•••	••••	••••	••••	•
Poland	•••	••••	••••	••••••	•
Portugal	•••	••••	••••	••••	•
Qatar	•••	••••	••••	••••	••
Russia	•••	••••	••••	••••	••
Singapore	•••	••••	••••	••••	•
South Africa	•••	••••	••••	••••	•
Spain	•••	••••	••••	••••	•
Sweden	•••	••••	••••	••••••	•
Switzerland	•••	••••	••••	••••••	•
Taiwan	•••	••••	••••	••••	•
Thailand	•••	••••	••••	••••	•
Turkey	•••	••••	••••	••••	••
UAE	•••	••••	••••	••••	••
UK	•••	••••	••••	••••	••
USA	•••	••••	••••	••••	•

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