IFPHK’s Response to the Hang Seng Indexes Company Limited (HSI) Consultation Paper on the Eligibility of Weighted Voting Right Companies and Secondary-listed Companies for Inclusion in the Hang Send Index

March 2020

Contents

Institute of Financial Planners of Hong Kong (IFPHK) - Profile

<u>Background</u>

The IFPHK was established in June 2000 as a non-profit organization for the fast-growing financial industry. It aims to be recognized in the region as the premier professional body representing those financial planners that uphold the highest standards for the benefit of the public.

The IFPHK is the sole licensing body in Hong Kong authorized by Financial Planning Standards Board Limited to grant the much-coveted and internationally-recognized CFP^{CM} certification and AFP^{TM} certification to qualified financial planning professionals in Hong Kong and Macau.

It represents more than 6,800 financial planning practitioners in Hong Kong from such diverse professional backgrounds as banking, insurance, independent financial advisory, stockbroking, accounting, and legal services.

Currently there are more than 147,000 CFP certificants in 24 countries/regions; the majority of these professionals are in the U.S., Canada, China, Australia and Japan, with more than 4,700 CFP certificants in Hong Kong.

CFP^{CM}, CERTIFIED FINANCIAL PLANNER^{CM}, CFP^{CM}, CERTIFIED FINANCIAL PLANNER ™, AFP^{TM}, ASSOCIATE FINANCIAL PLANNER^{TM}, AFP and ASSOCIATE FINANCIAL PLANNER® are certification marks and/or trademarks owned outside the U.S. by Financial Planning Standards Board Ltd. The Institute of Financial Planners of Hong Kong is the marks licensing authority for the CFP marks and AFP marks in Hong Kong and Macau, through agreement with FPSB.

<u>IFPHK's interest in this consultation</u>

The mission and vision of the IFPHK is to promote the importance of financial planning[1]. The IFPHK is the sole licensing body in Hong Kong authorized by the FPSB to grant the internationally recognized CFP^{CM} Certification and AFP^{TM} Certification to qualified financial planning professionals in Hong Kong and Macau.

As the leading professional body for the welfare of the financial planning industry, the IFPHK actively responds to policy changes that affect the industry or the financial system as a whole. A list of IFPHK responses to various consultation papers can be found on our website (http://www.ifphk.org/ee/importance-of-advocacy).

In 2016, IFPHK responded to the Join Consultation Paper on Proposed Enhancements to the Stock Exchange of Hong Kong Limited's Decision-making and Governance Structure for Listing Regulation Issued by the Securities and Futures Commission ("SFC") and the Stock Exchange of Hong Kong Limited ("HKEX"). We supported the proposals to enhance governance of the listing process. Also. IFPHK responded to HKEX's Consultation Paper on a Listing Regime for Companies from Emerging and Innovative Sectors in 2018.

[1] www.fpsb.org. Financial planning refers to the process of setting, planning, achieving and reviewing life goals through the proper management of finances.

In light of the above, IFPHK wishes to comment on the proposals set out in the Consultation Paper.

<u>IFPHK's representation</u>
IFPHK was founded by 30 members (the 'Founding Members') to raise the standards of financial planners and highlight the importance of sound financial planning.

IFPHK currently has 39 Corporate Members, including banks, independent financial advisors, insurance companies and securities brokerages. With our Corporate Members providing a full spectrum of client services and products, the IFPHK is well positioned to understand the needs, concerns and aspirations of the financial planning community.

Executive Summary

On 13 January 2020, the Hang Seng Indexes Company Limited (HSI), a wholly-owned subsidiary of Hang Seng Bank published a consultation paper seeking public feedback on the proposed new rules to change eligibility of weighted voting right companies and secondary-listed companies for inclusion in the Hang Seng Index ("consultation paper"). The public comment period ends on 13 March 2020.

Created in 1969, the Hang Seng Index was originally designed to represent the Hong Kong stock market by reflecting the performance of the largest and most liquid companies within the market. Over the past 50 years, the Hong Kong stock market has evolved and become significantly more layered and sophisticated. In recent years, the Stock Exchange of Hong Kong (SEHK) has revised the listing chapters to accommodate companies in innovative or new economy sectors.

Although financial planners are not directly affected by the proposed regime, the changes are significant for the financial service industry as a whole because publicly listed securities are major investment vehicles. In 2018, IFPHK provided feedback to consultation paper on proposed rules to expand Hong Kong's listing regime to facilitate listings of companies from emerging and innovative sectors. For this reason, the IFPHK would like to provide general comments on the proposals of the Consultation Paper.

Our comments are based on the following principles which are the same as our last consultation paper submission:

1. Assuring the quality of listed companies

Over the past two decades, many newly listed companies have later been deemed unfit for public listing. This unacceptably large proportion of failures reflects the shortcomings of the current voluntary-disclosure system in protecting investors' interests[2]. Hong Kong's position as a key IPO destination does not lie with the amount of funds raised or the number of new listings. Sustainable growth of the local stock market relies on the quality of its listed companies. Heightened concerns over growing IPO fraud and the deteriorating quality of listed companies have raised questions about whether or not the Exchange should continue its dual role as a for-profit company and a regulator of listed companies. Major international stock markets have, for many years, moved the responsibility for listing matters entirely to the securities regulator or an independent regulatory body, as in the US and the UK. Hong Kong is behind the curve in terms of having an independent regulator to administer listing matters. To our disappointment, the conflicting role of the Exchange has not been addressed in last consultation. The WVRs structure has been introduced without significant enhancement to corporate governance and investor protection.

2. Enhancing investor protection

The IFPHK supports a regulatory system that would facilitate delivering better financial products and services for the investing public as well as protecting them. The IFPHK is aware that many overseas companies are seeking a listing in Hong Kong to tap into the market for long-term

[2] Peter Liang, "Opinion: IPO reform – stockbrokers need to look at both sides of the coin, China Daily, 3 August 2016

institutional investment funds. To attract these companies, Hong Kong must maintain a transparent and well-regulated market. Effective consumer protection and a healthy balance between robust regulations and market development are our areas of focus.

The Exchange has a statutory duty to act in the interest of the investing public, but HKEx is also a listed company that polices the companies that provide its revenue and shareholder dividends. Such a dual role is not ideal. There are conflicts of interest that weaken investors protection.

3. Enhancing investor engagement and stewardship

The London Stock Exchange has established an independent body consisting of representatives from the regulatory sector, professionals, and the investing public, to vet IPO applications. The engagement of retail investors in Hong Kong, however, is almost non-existent. Retail investors hardly ever vote, despite the advances of technology and emergence of online brokers. Even the participation of institutional investors is not very active compared with the US. Principles of responsible ownership and investor stewardship are now widely discussed in the asset management industry. The Government and regulator should increase the engagement of retail investors and institutional investors.

4. Enhancing financial literacy and promoting financial education

Well-informed and educated consumers are core elements in a healthy regulatory system. For a market to perform effectively and for consumers to be protected properly, a fundamental understanding of how financial products work is essential. Given that such a high proportion of Hong Kong people invest in financial markets, especially securities, it is important for them to adopt and apply responsible attitudes towards investing and money management.[3] The IFPHK considers it effective and appropriate to empower, and improve the awareness of, investors through means such as investor education.

Compared to other exchanges, the Hong Kong's Exchange does relatively little in terms of promoting financial literacy and educating the investing public. Given the high participation of local investors in Hong Kong's securities markets, the Exchange has the responsibility to educate the public on shareholder's rights and the risks associated with securities products. The IFPHK urges the Exchange to spend more on, and invest more resources in, investor education.

IFPHK's comments are summarized as follows:

The engagement of retail investors in Hong Kong is almost non-existent and the current knowledge level of Hong Kong investors is inadequate. Few minority shareholders fully understand their rights, and the legal remedies against managerial misconduct available to shareholders in Hong Kong are very limited. Even for Exchange Traded Fund ("ETF") investors, it is not believed that they have competence of the index methodology and what are the constituents meant to them. Besides, our regulatory system does not offer the same protection to retail investors like those in US (e.g. fiduciary duty and class actions). Without significant changes to existing listing regime and investor protection system to tackle the emerging listing of companies with WVRs structure or from emerging market, IFPHK thus considers that

[3] Investor Education Council, press release on 23 July 2013.

- It is not the right timing to propose any change to the composite of the HSI
- Disagree to include WVRs into household index in Hong Kong including both HSI and HSCEI
- Disagree to include secondary-listed companies

Hong Kong's position as a key IPO destination does not lie in the amount of funds raised or the number of new listings. Sustainable growth of the local stock market relies on the quality of listed companies. There should be a proper balance between business development on one hand and good corporate governance on the other. The Exchange as a frontline regulator of listing matters must function effectively as a gatekeeper. Given its conflicted roles, suspicions that the Exchange's decisions are purely commercial is inevitable. We find it urgent that the Government address these concerns rather than propose any changes to the HSI.

The statements given in the IFPHK's response to the Consultation Paper are based on objective and independent analysis of market and consumer needs. To ensure that the IFPHK understands the concerns and practicality of the issue, it has sought comments from active industry practitioners who deal with this issue on a regular basis.

The HSI Consultation

On 13 January 2020, the Hang Seng Indexes Company Limited (HSI), a wholly-owned subsidiary of Hang Seng Bank published a consultation paper seeking public feedback on the proposed new rules to change eligibility of weighted voting right companies and secondary-listed companies for inclusion in the Hang Seng Index ("consultation paper"). The public comment period ends on 13 March 2020.

Created in 1969, the Hang Seng Index was originally designed to represent the Hong Kong stock market by reflecting the performance of the largest and most liquid companies within the market. Over the past 50 years, the Hong Kong stock market has evolved and become significantly more layered and sophisticated. In recent years, the Stock Exchange of Hong Kong (SEHK) has revised the listing chapters to accommodate companies in innovative or new economy sectors.

Following a market consultation in 2018, HSI seek views to broaden the eligibility universe of the Hang Seng Composite Index ("HSCI") to include foreign companies, stapled securities and WVRs. As such, in this consultation paper, HSI wishes to solicit market feedback on 12 questions in 5 areas:

1. The positioning of the HSI;

Question 1: What do you think the HSI should now represent given the significant development and evolution of Hong Kong stock market over the past 50 years?

Question 2: Do you think there is a need to maintain a reasonable balance between Hong Kong and non-Hong Kong constituents in the HSI?

Question 3: How would you rank the following considerations in deciding changes of HSI constituents?

2. The eligibility of WVRs for the HSI;

Question 4: Do you think WVRs should be eligible for inclusion in the HSI?

Question 5: If WVRs are to be added to the HSI, do you think there is any need to limit their proportion in the index?

3. The eligibility of secondary-listed companies for the HSI;

Question 6: Do you think secondary-listed Greater China companies should be eligible for inclusion in the HSI?

Question 7: If secondary listed Greater China companies are to be added to the HSI, do you think there is any need to limit their representation in the index?

4. The weighting of the Financial sector in the HSI;

Question 8: Do you think the weighting of the Financials sector in the HSI is an issue that needs to be addressed?

Question 9: Is sector capping a good way to prevent any sector(s) from overly dominating the HSI?

5. Matters related to the HSCEI

Question 10: Do you think WVRs should be eligible for inclusion in the HSCEI?

Question 11: Do you think secondary-listed companies should be eligible for inclusion in the HSCEI?

Question 12: Should the extra eligibility conditions that currently apply to Red-chips and P-chips be removed?

IFPHK's Submission

The views expressed in this submission paper are not necessarily simply summaries of the views taken from the industry. They have undergone independent and critical analysis and consideration by the IFPHK as a professional body. As a result, not all the views collected by the IFPHK are recorded in this submission paper. Nor have all the views expressed in this paper been directly endorsed by the industry representatives or members consulted. The IFPHK takes the practical implications of the proposed changes for the work of financial planners, who advise and provide professional services to investors, as its utmost priority.

In considering the various proposals of the Consultation Paper, the IFPHK's comments are based upon the following principles and beliefs:

IFPHK's Principles

1. Assuring the quality of listed companies

Over the past two decades, many newly listed companies have later been deemed unfit for public listing. This unacceptably large proportion of failures reflects the shortcomings of the current voluntary-disclosure system in protecting investors' interests[4]. In 2010, the Chief Executive of China Forestry was arrested. The SFC asked the court to freeze around HK$400 million of his assets as potential reparation to investors. Another company, the Chinese fabric maker Hontex, was accused by the SFC of issuing a prospectus containing false and misleading information. Hontex agreed in June 2012 to repay more than HK$1 billion to investors. In 2015, the Exchange cancelled China Metals Recycling Holdings' seven-year-old listing. According to HKEx, the company obtained its initial listing by fraud and so was no longer suitable for listing[5]. In view of the seriousness of the IPO fraud, the SFC immediately reformed the IPO sponsor regime. Recent actions against the financial company Convoy Global again raised concerns over the quality of listed companies.

Hong Kong's position as a key IPO destination does not lie with the amount of funds raised or the number of new listings. Instead, the sustainable growth of the local stock market relies on the quality of listed companies. As we highlighted in our last submission to HKEX, for many years, major international stock markets have moved the responsibility for listing matters entirely to a securities regulator or an independent regulatory body, as we have seen in the US and the UK. In our view, Hong Kong is behind the curve in that it has not developed an independent regulator to administer listing matters.

2. Enhancing investor protection

The IFPHK supports a regulatory system that facilitates delivering better financial products and services for the benefit of the investing public, as well as protecting them. The IFPHK is aware that many overseas companies are seeking a listing in Hong Kong to tap into the market for long-term institutional investment funds. To attract these companies, Hong Kong must maintain a transparent and well-regulated market. For that reason, effective consumer protection and a healthy balance between robust regulations and market development are our areas of focus.

[4] Peter Liang, "Opinion: IPO reform – stockbrokers need to look at both sides of the coin, China Daily, 3 August 2016

[5] Peter Guy, "Mainland Chinese define fraud differently, and Hong Kong regulators should wake up", SCMP, 14 January 2016

As highlighted in our previous submission on Consultation of listing regime, while the Exchange has a statutory duty to act in the interest of the investing public, HKEX is a listed company and polices the companies that provide its revenue and shareholder dividends. Such a dual role is not ideal and involves conflicts of interest. Given increasing demand for better corporate governance, the IFPHK notes that there is inevitable and growing criticism that, as a publicly-listed company, the Exchange puts too much emphasis on the interests of its shareholders and members and too little on fulfilling its fiduciary duty to the public as a monopoly[6]. To better protect retail investors, measures should be taken to address the conflicting roles of the Exchange.

To our disappointment, the conflicting role of the Exchange has not been addressed in last consultation. The WVRs structure has been introduced without significant enhancement to corporate governance and investor protection.

3. Enhancing investor engagement and stewardship

The London Stock Exchange has established an independent body consisting of representatives from the regulator, professionals and the investing public to vet IPO applications. The engagement of retail investors in Hong Kong, however, is almost non-existent. Retail investors hardly ever vote, despite advances of technology and the emergence of online brokers. The Government and regulator should consider encouraging greater engagement of retail investors. Compared to the US, there is even relatively low participation of institutional investors. The principles of responsible ownership and active investor stewardship are widely discussed in the asset management industry.

Investor stewardship is a global trend. For example: more companies are signing on to the Japan Engagement Consortium (led by Governance for Owners Japan). There is a growing sense that Japanese firms are more willing to engage with investors, even as investors become more active. This is evidenced by the way that Japan’s Government Pension Investment Fund (GPIF) has taken on a leadership role regarding domestic asset owners[7].

At present, this kind of investor engagement and stewardship is still immature in Hong Kong despite of the size and liquidity of our stock market.

4. Enhancing financial literacy and promoting financial education

Well-informed and educated consumers are the core elements in a healthy regulatory system. For a market to perform effectively and for consumers to be protected properly, a fundamental understanding of how financial products work is essential. It is the IFPHK’s view that improved financial literacy levels will not only allow consumers to make more informed investment decisions, but also result in greater consumer appreciation of the need to plan a long-term financial future, a concept the IFPHK continually advocates. Given the high degree of participation of Hong Kong people in financial markets, especially securities, it is important for them to adopt and apply responsible attitudes towards investing and money management. The IFPHK considers it effective and appropriate to empower and improve investors through means such as investor education.

[6] Peter Liang, “Opinion: IPO reform – stockbrokers need to look at both sides of the coin”, 3 August 2016, China Daily
[7] Global and Regional Trendsin Corporate Governance for 2018, Russell Reynold Associate

Questions raised in the Consultation Paper

1) Positioning of the HSI

Question 1:

What do think the HSI should now represent given the significant development and evolution of Hong Kong stock market over the past 50 years? (Select one answer only)

- **Largest and most liquid Hong Kong-listed stocks, regardless their geographical exposure or nationality (potentially also include foreign companies)**
- **Listed companies from Greater China region (i.e. Hong Kong, Mainland, Macau and Taiwan)**
- **Hong Kong-listed companies that reflect the Hong Kong economy**
- **Others, please specify.**

Please provide your reasons, comments and suggestions

<u>IFPHK Responses</u>
IFPHK considers that the HSI shall reflect Hong Kong economics performance, and Hong Kong listed companies shall be more representatives of Hong Kong economy.

As mentioned in our last submission to HKEX on listing regime, the engagement of retail investors in Hong Kong is almost non-existent. Besides, the current knowledge level of Hong Kong investors is inadequate. Few minority shareholders fully understand their rights, and the legal remedies against managerial misconduct available to shareholders in Hong Kong are very limited. Even for Exchange Traded Fund (“ETF”) investors, it is not believed that they have competence of the index methodology and what are the constituents meant to them. As a result, investors mainly rely on the index due diligence process conducted by the ETF managers. If the index is composed of complicated structures for example stocks with WVR and secondary listing, and which no such mandatory voting system (under fiduciary duties) for the ETF managers, investors’ benefits will be at risk.

Compared to other exchanges, the Exchanges do relatively little to promote financial literacy and educate the investing public. The Investor Education Centre is a cross-sectoral investor education body aimed at improving the financial knowledge and capability of the general public. However, given the high participation of investors in securities markets, the Exchange does have the responsibility to educate the public on shareholder’s rights and the risks associated with securities products.

From an investor protection point of view, the HSI shall reflect Hong Kong economics. Hong Kong is an international financial centre with free minimum controls, sophisticated investors can invest in other securities market directly if they have knowledge of international economy.

Question 2:

Do you think there is a need to maintain a reasonable balance between Hong Kong# and non-Hong Kong constituents in the HSI? (select one answer only)

- **Yes, there should be a reasonable balance between Hong Kong and non-Hong Kong constituents in the HSI in terms of (select one answer only)**
  - **Number of constituents**
  - **Weighting for Hong Kong and non-Hong Kong constituents**
- **No, the natural distribution of Hong Kong and non-Hong Kong constituents in the HSI according to the existing**

 # "Hong Kong" companies are those companies that are not foreign companies or Mainland companies as defined by Hang Seng Indexes.

<u>IFPHK Responses</u>

As mentioned in Question 1, we consider that the investor engagements and investor education are immature to impose changes to existing methodology. Take reference to international stock exchange like NASDAQ. For a security to be considered for listing in the NASDAQ Composite, the security must be exclusively listed on the NASDAQ Stock Exchange.

As we highlighted in our previous consultation submission, the IFPHK wish to find a balance between high growth and corporate governance standards. As aforementioned minority shareholders are certainly placed in a less favourable position under a WVR structure. However, even under the existing "one-share, one vote" structure, the engagement of retail investors in Hong Kong is almost non-existent. Few minority shareholders fully understand their rights, and the legal remedies against managerial misconduct available to shareholders in Hong Kong are very limited.

We highlight in our previous submission that the critical issue lies with the corporate governance of the listing process. Our major concern is the dual and conflicted role of HKEx and the Exchange. Such conflicting roles (a regulator administering the Listing Rules as well as acting as a for-profit exchange) give rise to doubts about whether the decisions of the Exchange are in the best interests of investors. Stock exchanges in the United States are not market regulators. Therefore it is understandable that they establish their listing criteria solely on a commercial basis. Also, the SFC does not have similar powers to those of the SEC. The SEC has the power to enforce federal securities laws. The IFPHK thinks that in the long run a complete segregation of the Exchange's regulatory functions from its commercial and operating activities is needed. This will align with international best practice and to avoid conflicts of interest that jeopardise investors' interests.

In terms of investor engagement, the London Stock Exchange has established an independent body consisting of representatives from the regulator, professionals, and the investing public, to vet IPO applications. We cannot find such minority investors engagement in Hong Kong.

Question 3:

How would you rank the following considerations in deciding change of HSI constituents? (1 – most important; 3 – least important)

- **Market representatives – for transparency's sake the largest and most liquid companies should be selected even if they may qualify as constituents at their peak price.**
- **Growth potential – tech-related or emerging sector companies that may not be among the largest stocks but that may possess longer term potential should not be disadvantaged in constituent selection.**
- **Others (e.g. fundamental criteria, ESG performance, etc.), please specify**

<u>IFPHK Responses</u>
IFPHK rank the following considerations in deciding changes of HSI constituents:

1. Others criteria like ESG performance
2. Market representatives – for transparency's sake the largest and most liquid companies should be selected even if they may qualify as constituents at their peak price.
3. Growth potential - tech-related or emerging sector companies that may not be among the largest stocks but that may possess longer term potential should not be disadvantaged in constituent selection.

Environmental, Social and Governance (ESG) has evolved and moved from the sidelines to the forefront of decision-making for asset managers and institutional investors. Responsible investing is widely understood as the integration of environmental, social and governance (ESG) factors into investment processes and decision-making. More and more believe that ESG factors have relevancy to financial results. Sophisticated investors recognize that ESG information about corporations is vital to understand corporate purpose, strategy and management quality of companies. It is now, quite literally, big business. ESG criteria is vital and relevant to sustainability growth potential. They assess an organization's resilience, adaptability, long-term sustainability and capacity for growth.

$17.5tn out of the $79tn of total assets under management globally are invested in funds applying environmental social and governance criteria.[8] Asia is lag behind in ESG development. Post coronavirus crisis would lead to awakening of governments and corporations in Asia on ESG criteria and sustainable investing.

[8] Asia overtake the West in sustainable investing, Helene Li and Curtis Chin, 26 February 2020, Financial Times

2) Eligibility of WVRs for the HSI

The first WVR listed in Hong Kong in July 2018. As at the end of 2019, there were three AVRs listed in Hong Kong. These entities are usually large technology-related Mainland companies with global business interests. From the perspective of market representation, it seems inappropriate to exclude these large-cap companies from key benchmark indexes. On the other hand, opponents have raised concerns about the unequal voting right structure of WVRs, which might disadvantage general shareholders given the superior voting rights of certain "minority" shareholders.

Question 4:

Do you think WVRs should be eligible for inclusion in the HSI?

- **Yes, WVRs should be eligible**
- **No, WVRs should not be eligible unless they meet additional criteria**
- **No, WVR should ever be eligible**

<u>IFPHK Responses</u>

From our principles of investor protection and financial literacy, WVRs with a different voting right structure and different governance structure shall not be included in the index.

As aforementioned, minority investor protections and investor education on listing and securities matters are still not optimal. As mentioned in our previous consultation paper submission, two major systems in place in US to ensure adequate governance towards the power of management with WVRs. Firstly, the fiduciary duties of licensed entities would ensure all intermediaries (both advisors and asset managers) would take the best interest of investors into account. Asset managers are responsible to vote on their investors behalf based on the best of investors. Even for minority interests, investors can still go for class actions to pursue remedies if their rights were misappropriated by the management that held weighted voting power.

Furthermore, knowledge of investors is insufficient. Very few understand their right and even less investors know the methodology behind the index. If the regulators do not plan to implement adequate investor protection system to tackle the emerging listing of companies with WVR, IFPHK thinks it is not the right time to include companies with WVRs into the household index in Hong Kong.

Question 5:

If WVRs are to be added to the HSI, do you think there is any need to limit their proportion in the index?

- **Yes, WVR constituents should be limited in terms of**
    - **Total number of constituents**
    - **Aggregate weighting in the HSI**
    - **Discounted individual weighting (e.g. adopt a common discount factor of 0.5 to all WVR constituents)**
- **No, WVRs should be treated the same as other HSI constituents**

<u>IFPHK Responses</u>

Owing to the response in Question 4, we skip this question.

3) Eligibility of Secondary-listed Companies for the HSI

Primary-listed companies are fully subject to the listing rules of the SEHK. In contrast, secondary-listed companies are principally regulated by the jurisdiction where they are primary listed. Certain SEHK listing rules are waived for secondary listings based on an understanding that shareholder protection standards that are in place in the overseas primary market are at least as stringent as those in Hong Kong.

Question 6:

Do you think secondary-listed Greater China companies should be eligible for inclusion in the HSI?

- **Yes, secondary-listed Greater China companies should be eligible**
- **No, secondary-listed companies should not be eligible unless they meet additional criteria.**
- **No, secondary-listed companies should never be eligible**

<u>IFPHK Responses</u>

IFPHK thinks secondary-listed companies should never be eligible. Based on principles of investor protection, IFPHK considers it is still premature to expand the scope of HSI to secondary-listed companies. Also it is not very common for index to include secondary-listed companies. Take reference to international stock exchange like NASDAQ. For a security to be considered for listing in the NASDAQ Composite, the security must be exclusively listed on the NASDAQ Stock Exchange.

Question 7:

If secondary-listed Greater China companies are to be added to the HSI, do you think there is any need to limit their representation in the index?

- **Yes, secondary-listed constituents should be limited in terms of**
    - **Total number of constituents**
    - **Aggregate weighting in the HSI**
    - **Discounted individual weighting**
- **No, secondary-listed companies should be treated the same as other HSI constituents**

<u>IFPHK Responses</u>

As we disagree to include secondary-listed companies, IFPHK would skip this question.

4) Weighting of the Financial Sector in the HSI

Financials has been a dominant segment in the HSI for some time. As at the end of 2019, there were 11 finance stocks in the index, which collectively accounted for nearly half of the index weighting. Since 2010, a growing number of market participants have begun to express concerns over the heavy weighting of Financials in the HSI . As such, HSI expose the possibility to adopt sector capping i.e. set a ceiling for the allowable aggregate weighting for any sector in the HSI.

Question 8:

Do you think the weighting of the Financials sector in the HSI is an issue that needs to be addressed?

- **Yes, I think it should be addressed**
- **No, I do not consider this is an issue**

<u>IFPHK Response</u>
IFPHK do not think there is a problem of current weighting of the financial sectors if the index generally reflects the economic performance of Hong Kong.

Question 9:

Is sector capping a good way to prevent any sector(s) from overly dominating the HSI?

- **Yes, I think it would help resolve the problem**
- **No, I believe other methods would be more effective**
    - **Limiting the number of constituents in any particular sector**
    - **Applying sector-specific caps on individual constituent weightings (e.g. 8% for Financials constituents, 10% for constituents in other sectors)**
    - **Others, please specify**

<u>IFPHK Response</u>
Based on our response of Question 8, we would skip this question.

5) Matters related to the HSCEI

Similar to the HSI , the HSCEI index universe does not currently include WVRs and secondary-listed companies. Given recent market developments, it is expected that there will be more Mainland WVRs and/ or secondary-listed companies be listed in Hong Kong. To continue to exclude these companies from the HSCEI may therefore have an increasingly significant adverse effect on the HSCEI's representativeness as the "China Index of the Hong Kong Market".

Question 10:

Do you think WVRs should be eligible for inclusion in the HSCEI?
- **Yes, WVRs should be eligible**
- **No, WVRs should not be eligible**

Question 11:
Do you think secondary-listed companies should be eligible for inclusion in the HSCEI?
- **Yes, secondary-listed companies should be eligible**
- **No, secondary-listed companies should not be eligible**

<u>IFPHK Response</u>
Hong Kong's position as a key IPO destination does not lie with the amount of funds raised or the number of new listings. Instead, the sustainable growth of the local stock market relies on the quality of listed companies. In additions, the engagement and literacy of minority investors have not been improved since the change of the listing regime.

Based on the principles of investor protection, we disagree to include WVRs and secondary-listed companies to HSI as well as HSCEI.

Question 12

Should the extra eligibility conditions that currently apply to Red-chips and P-chips be removed?
- **Yes, the extra eligibility conditions that currently apply to Red-chips and P-chips should be removed.**
- **No, the extra eligibility conditions that currently apply to Red-chips and P-chips are fine and there is no need to make any changes at this time**

<u>IFPHK response</u>
Unless there are significant measures to enhance investors engagement and financial literacy of minority investor, IFPHK do not support to impose change to the methodology of both HSI and HSCEI.