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Traders Education: FTSE Xinhua 25 Index changes

(For the list of FTSE Xinhua 25 Index, please go to http://us.ishares.com/product_info/fund/holdings/FXI.htm)

Picking shares on index changes

Changes of FTSE Xinhua 25 Index in Q4 will be announced on 6 October. ABC (1288) listed in July was only included in FTSE Xinhua Hong Kong Index for it was too quick to incorporate the bank into FTSE Xinhua 25 Index then. Therefore, ABC is the hot pick for the quarterly review this time.

Previously, some major brokers pointed out that ABC, as a state-owned enterprise and a red chip company, was very likely to be included in the index, while Datang Power, as the company with the smallest capitalization in the index, will be excluded.

The report said that approximately HK\$86.9b is tracking FTSE Xinhua 25 Index in the market. If ABC is included, the buying amount of index fund is estimated to be around \$3.5b, or nearly 900m shares. At the 20-day average turnover amount, passive funds need to buy 3.3-day turnover amount. And passive funds are believed to sell about \$680m Datang Power, or 200m shares, which is equivalent to 6.7-day turnover amount.

The proportion of components in the index may be adjusted as well. CNOOC may be raised and the passive buy-in amount is around HK\$2.25b, i.e. approximately 150m shares or 2.7-day turnover. Proportions of China Communications Construction (1800), China Railway (390), CITIC Bank (998) and Bank of China (3988) will be lowered. The shares of China Communications Construction to be sold are about 36.4m, or 2.7-day turnover amount; shares of China Railway to be sold are estimated to be 35m, or



2.0-day turnover amount. Shares of CITIC Bank to be sold are about 77.4m, or 1.9-day turnover amount. Shares of Bank of China to be sold are estimated to be 370m, or 1.9-day turnover amount.

Action	Company	Amount (million HK\$)	Number of shares	Average turnover day
Include	ABC	3,477	898.4	3.3
Exclude	Datang Power	-677.7	-204.8	6.7
Raise	CNOOC	2,249	154.5	2.7
Lower	China Communications Construction	-264.3	-36.4	2.3
Lower	China Railway	-208.6	-35.0	2.0
Lower	CITIC Bank	-387.0	-77.4	1.9
Lower	Bank of China	-1504	-369.6	1.9

Recommendation

Recommend to buy ABC for short-term trading. The index change will be effective on 18 October. Index funds are believed to act on 15 October, it should be sold on or before 15 October. If, unfortunately, it is not included, it should be sold as well. At the same avoid buying Datang Power, China Communications Construction, China Railway, CITIC Bank and Bank of China.

(My clients hold ABC (1288))