

MarketGrader New China ESG Index
Rulebook and Methodology Overview
2021



MarketGrader
RESEARCH & INDEXES

Introduction

The MarketGrader New China ESG Index (the “Index”), created and maintained by MarketGrader, is designed to provide investors with exposure to the most financially sound companies domiciled in China that are listed on one or more of the following exchanges:

- a. The Mainland China Stock Exchanges (Shanghai Stock Exchange and Shenzhen Stock Exchange) that are accessible to foreign investors through the Hong Kong Stock Connect program (Northbound and Southbound).
- b. The Hong Kong Stock Exchange.
- c. The United States National Exchanges (the New York Stock Exchange and NASDAQ).

In addition, the companies selected into the Index are compliant (above median performers) with Environmental, Sustainability and Governance (ESG) criteria based on the OWL Analytics consensus ESG Score. OWL ESG covers over 25,000 companies globally, publishing metrics monthly that are aggregated from hundreds of independent ESG data sources. OWL ESG scores and ranks all companies in its coverage universe across thirty core metrics, including 12 key performance indicators (KPIs) that quantify company behavior across Environmental, Social and Governance factors.

MarketGrader reconstitutes the Index components on a semi-annual basis according to the methodology described in this document. The MarketGrader New China ESG Index is calculated and disseminated by Refinitiv and denominated in USD and EUR.

MarketGrader Research Universe

In order to define the universe from which the Index components are selected, it is necessary to first define the coverage of the MarketGrader Research Universe since the Index methodology performs security selection based on the company ratings calculated and published by MarketGrader Research.

The MarketGrader Research Universe is defined as the set of companies traded on public stock exchanges globally that meet the criteria necessary for MarketGrader to perform an in-depth comprehensive fundamental analysis on every company as defined in its proprietary ratings methodology. This methodology is based on 24 indicators, each graded independently, across four fundamental categories: Growth, Value, Profitability and Cash Flow. After grading each company on the 24 indicators, the sum of the grades is normalized into a MarketGrader Score (MG Score) ranging between zero and 100. This MG Score is the basis of the company ratings. To be able to compute the MG Score, MarketGrader therefore requires that a minimum number of fundamental indicators be available for every company in its universe. Furthermore, a minimum number of them must be available consistently over time for a company to be eligible for coverage by MarketGrader. The following criteria are implemented by MarketGrader in the maintenance of its research universe within each of MarketGrader’s primary geographic regions.

Americas:

The MarketGrader Research Universe includes all public issues defined as common shares and ADRs (American Depositary Receipts) that are listed in non-OTC (over the counter) exchanges. This includes Limited Partnerships (LPs) and Real Estate Investment Trusts (REITs). LPs and REITs are ineligible for inclusion to some indexes on a case-by-case basis. All issues eligible for universe inclusion must have at least three active trading days within the last 12 calendar days. Company domicile is defined based on the Entity “ISO Country” code as defined by FactSet.

Asia Pacific:

The MarketGrader Research Universe includes all public issues defined as common shares where, according to FactSet, entity types are defined as “public” or “holding companies”. Also, all entity sub-types defined as “Limited

Partnership”. All issues eligible for universe inclusion must have at least one active trading day within the last 12 calendar days. Company domicile is defined based on the Entity “ISO Country” code as defined by FactSet.

Europe & Middle East:

The MarketGrader Research Universe includes all public issues defined as common shares where, according to FactSet, entity types are defined as “public” or “holding companies”. Also, all entity sub-types defined as “Limited Partnership”. Only primary listing issues in this region are included in its research universe. All issues eligible for universe inclusion must have at least three active trading days within the last 12 calendar days. Company domicile is defined based on the Entity “ISO Country” code as defined by FactSet.

Across all geographic regions, the MarketGrader Research Universe excludes:

- Companies with zero trailing 12-month revenue and a total market capitalization below USD 500 million.
- Companies with zero annual revenue and a total market capitalization below USD 500 million.
- Companies with zero trailing 12-month revenue and annual sales older than two years prior to the universe evaluation date.
- Companies missing trailing 12-month revenue and annual revenue from most recently reported financial statement.
- Companies with ratings in less than 22 of MarketGrader’s 24 fundamental indicators.
- Companies whose most recently filed financials statements are over 12 months old from the date of the universe evaluation date.

Review Frequency

The MarketGrader Research Universe is reviewed on a weekly basis, following the last weekly close of equity markets in the U.S.

MarketGrader's New China ESG Index Selection Universe

The selection universe for the Index is comprised of all public issues from the MarketGrader Research Universe trading on Mainland China, Hong Kong and US Exchanges with the issuing company domiciled in China according to the entity "ISO Country" code defined by FactSet. In addition, issues trading on the Mainland China Exchanges have to be a part of the Hong Kong Stock Connect Program.

Companies within the selection universe for the Index must have received a MarketGrader overall rating consistently for at least six months. If a company is listed in a country with quarterly financial filing requirements, it should have reported the most recent financials within the last six months to be eligible for selection into the Index. If a company is listed in a country with semi-annual financial filing requirements, it should have reported the most recent financials within the last 12 months to be eligible for selection into the Index.

Since the Index focuses on the growth sectors of China's economy, only companies from the Consumer Discretionary, Consumer Staples, Health Care and Technology sectors, as identified by the MarketGrader Global Classification System, are eligible for the selection universe into the Index.

Finally, the companies within the selection universe must satisfy the following requirements:

- The company's stock cannot be classified as a "ST" (special treatment) stock by the China Securities Regulatory Commission (CSRC).
- If a company's stock is temporarily suspended from trading, it is ineligible from inclusion in the Index's selection universe.
- The company's stock Foreign Ownership on the selection date cannot exceed 26% of its free float adjusted market capitalization¹.
- The company may not appear in any of the U.S. Department of the Treasury's Office of Foreign Assets Control (OFAC) Sanctions Lists.
- The company may not appear in the U.S. Department of Defense list of "Qualifying Entities Prepared in Response to Section 1237 of the National Defense Authorization Act for Fiscal Year 1999."

Companies from the MarketGrader Research Universe passing the above criteria comprise the MarketGrader New China ESG Index Selection Universe.

¹ Foreign Ownership Limit Thresholds are based on figures published daily by the Shanghai Stock Exchange and the Shenzhen Stock Exchange.

The MarketGrader New China ESG Index Rules

Introduction

The MarketGrader New China ESG Index consists of 100 fundamentally sound companies domiciled in China and traded publicly in the Shanghai Stock Exchange, the Shenzhen Stock Exchange, the Hong Kong Stock Exchange or on U.S. National Exchanges. The index constituents are selected on the basis of the strength of their fundamentals as measured by the MarketGrader Score (0 to 100) and must rank above their regional sector median ESG composite score, as measured by OWL Analytics.

Index Name and Index Codes

Price Return Series

- Index Name: MarketGrader New China ESG Index – Price Return
- Short Name: MG New China ESG
- Index Codes: MGNCUSPR (USD Series) ; MGNCEUPR (EUR Series)

Net Total Return Series

- Index Name: MarketGrader New China ESG Index – Net Total Return
- Short Name: MG New China ESG – NTR
- Bloomberg and Reuters Code: MGNCUSNR (USD Series)
- Other Index Code: MGNCEUNR (EUR Series, not on Bloomberg)

Total Return Series

- Index Name: MarketGrader New China ESG Index – Total Return
- Short Name: MG New China ESG – TR
- Index Code: MGNCUSTR (USD Series); MGNCEUTR (EUR Series)

Base Date and Base Index Level

The Index's base date is December 31, 2007. Its base level is 100.

Index Reconstitution and Rebalance Dates

The Index is reconstituted and rebalanced after the close of trading on U.S. exchanges on the third Friday of March and September. The Index constituents are selected on the Tuesday of the previous week, or ten (10) calendar days prior to the reconstitution and rebalance date. Constituents are equally weighted on the Friday following the selection date and one week prior to the Index's official rebalance date.

Index Methodology

1. Investable Universe

All companies in the MarketGrader New China ESG Index Selection Universe (as defined above) are eligible for selection into the Index, provided they meet the investability criteria that are applicable at the time of the Index's reconstitution and rebalance.

Starting at inception (December 31, 2007) and for the next four reconstitutions and rebalances (through September 2009) of the Index, all companies in the MarketGrader New China ESG Index Selection Universe were eligible for selection into the Index, provided they met the following investability criteria:

- The company had a market capitalization of at least USD 200 million.
- The company's stock had a 3-month average trading volume of at least USD 2 million.
- The company's float factor was greater than 10%.

Starting in the March 2010 reconstitution and rebalance and for all reconstitutions and rebalances thereafter, all companies in MarketGrader New China ESG Index Selection Universe are eligible for selection into the Index, provided they meet the following investability criteria at the time of the Index's reconstitution and rebalance:

- The company has a market capitalization of at least USD 500 million.
- The company's stock has a 3-month average trading volume of at least USD 5 million.
- The company's float factor is greater than 10%.

The companies from the MarketGrader New China ESG Index Selection Universe passing the above criteria comprise the MarketGrader New China ESG Index Investable Universe.

2. Selection of Index Constituents

MarketGrader implements a proprietary methodology based on 24 indicators, each graded independently, across four fundamental categories: Growth, Value, Profitability and Cash Flow, which seeks to identify the companies with the strongest fundamentals. After grading each company on the 24 indicators, the sum of the grades is normalized into a MarketGrader Score (MG Score) ranging between zero and 100. Each company in the MarketGrader New China ESG Index Investable Universe has a MG Score.

Starting at inception (December 31, 2007) and for the next four reconstitutions and rebalances (through September 2009) of the Index, MarketGrader selected the 80 highest ranking MG Score companies from the MarketGrader New China ESG Index Investable Universe as components for the Index subject to the following criteria:

- No more than 24 companies could belong to any one sector.
- Existing components continued to be a part of the Index as long as their MG Score does not fall below the 96th ranked company (20% buffer for the MG Score).
- If an index constituent was dual listed in more than one of the exchanges in the Investable Universe and the non-constituent issue had a higher MarketGrader Score than the Index constituent, the Index constituent remained in the Index and was not replaced by the other issue even if the latter had a higher MarketGrader Score.
- If two issues of the same company with a dual listing were eligible for selection to the Index based on their MarketGrader Score (provided that one is not already an Index constituent), MarketGrader selected the issue with the higher three-month average daily trading volume (in USD) for inclusion in the Index.

Starting in the March 2010 reconstitution and rebalance of the Index and for all reconstitutions and rebalances thereafter, MarketGrader selects the 100 highest ranking MG Score companies from the MarketGrader New China ESG Index Investable Universe as components for the Index subject to the following criteria:

- No more than 30 companies may belong to any one sector.
- Existing components continue to be a part of the Index as long as their MG Score does not fall below the 120th ranked company (20% buffer for the MG Score).
- If an index constituent is dual listed in more than one of the exchanges in the Investable Universe and the non-constituent issue has a higher MarketGrader Score than the Index constituent, the Index constituent

will remain in the Index and not be replaced by the other issue even if the latter has a higher MarketGrader Score.

- If two issues of the same company with a dual listing are eligible for selection to the Index based on their MarketGrader Score (provided that one is not already an Index constituent), MarketGrader will select the issue with the higher three-month average daily trading volume (in USD) for inclusion in the Index.

Additionally, starting in the September 2018 reconstitution and rebalance of the Index and for all reconstitutions and rebalances thereafter, companies selected into the MarketGrader New China ESG Index Selection Universe need to satisfy the following ESG criteria:

- New components selected into the Index must be ranked in the top 50% within their regional peer group on an ESG consensus rating calculated by OWL Analytics.
- Existing components of the Index must be ranked in the top 66% within their regional peer group on an ESG consensus rating calculated by OWL Analytics.

OWL ESG scores and ranks all companies in its coverage universe across thirty core metrics, including 12 key performance indicators (KPIs), that quantify company behavior across Environmental, Social and Governance factors. A complete description of OWL's ESG rating methodology is available in the "OWL ESG Brochure."²

OWL then separates all companies under coverage into 361 peer groups, which are designated by one of three factor pairs—Region and Industry, Region and Subsector, or Region and Sector. A company can belong to at most three peer groups. For every company under coverage, OWL provides their monthly rank and percentile within their appropriate peer group(s) in every one of OWL's ESG metrics. This allows MarketGrader to identify how a company compares to its peers across all metrics in the relevant region. For the MarketGrader New China ESG Index, the peer group is defined as the set of all companies belonging to the same sector that are domiciled in any Emerging Economy in the Asia Pacific Region, as defined by the International Monetary Fund's (IMF) World Economic Outlook Database³, and covered by OWL Analytics.

3. Foreign Ownership Limit Rules

If at any time the free float adjusted market capitalization of an Index constituent reaches a foreign ownership percentage of 26%, the stock will be put on a Foreign Ownership Limit (FOL) watch list for possible deletion at the 27% threshold. If the stock reaches the 27% threshold, it will be deleted from the Index on the fourth trading day following the first day it reached such threshold. The stock will then be deleted from the Index with a presumed market value per unit of stock equal to the closing price on its last trading day and the proceeds will be reinvested across the remaining Index constituents proportionally to their weights on the date the deletion is announced.

4. Stock Connect Program

If at any time an Index constituent that trades on one of China's Mainland stock exchanges (Shanghai Stock Exchange or Shenzhen Stock Exchange) through the Hong Kong Stock Connect Program is moved to the 'Sell Only' list (which means that foreign investors can only sell but not buy the stock through the Connect Program), it will be deleted from the Index. The deletion will take place on the fourth trading day following the announcement that the stock was moved to the 'Sell Only' list. The stock will then be deleted from the Index with a presumed market value per unit of stock equal to the closing price on its last trading day and the proceeds will be reinvested across the remaining Index constituents proportionally to their weights on the date the deletion is announced.

² <http://owlanalytics.net/>

³ <https://www.imf.org/en/Publications/WEO>

5. Constituent Weighting Methodology

All Index constituents are equally weighted on the Friday following the selection date and one week prior to the Index's official rebalance date.

Index Calculation Agent, Index Calculation Methodology and Corporate Actions

The Index's calculation agent is Refinitiv Indices. The Index is calculated according to the Refinitiv Global Equity Indices divisor driven methodology, available [here](#). Corporate actions are handled according to the Refinitiv Equity Indices Corporate Action Methodology, available [here](#).