China's Onshore Equities Beyond Large Caps: The S&P China A MidCap 500 Index

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Introduction

The S&P China A MidCap 500 Index seeks to provide representative exposure to mid-sized China A-shares while requiring positive earnings for index constituents and excluding sanctioned securities. The index composition provides differentiated exposure when compared to the large-cap-focused S&P China A 300 Index due to the unique characteristics of the mid-cap size category.

In this overview, we will explore why one may want to consider mid-cap China A-shares, including:

- Their limited representation in conventional China and emerging market benchmarks;
- The size and scope of the opportunity set;
- Differentiated investment characteristics and high return dispersion compared to large-cap A-shares; and
- A combination of both large-cap and mid-cap exposure provides broader coverage across sectors.

The methodology of the S&P China A MidCap 500 Index offers some additional potential benefits, including:

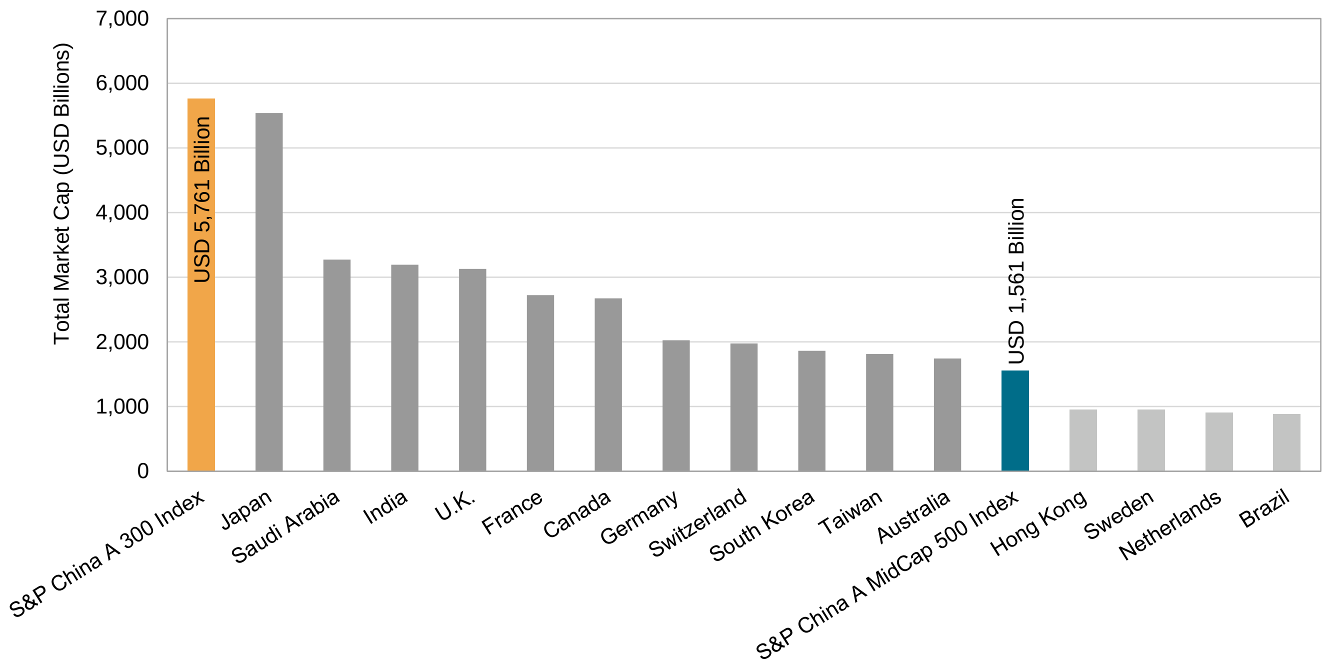
- A profitability requirement to eliminate companies lacking a track record of generating positive earnings; and
- The exclusion of sanctioned securities.

The Size and Scope of China A-Shares

While Chinese equities have grown in importance for international market participants, A-shares are limited to partial inclusion factors within broad benchmarks, leaving them significantly underrepresented in conventional Chinese and emerging market indices. Without representative inclusion of A-shares, China-specific exposure within indices could be considered incomplete.

Given the size and depth of China's onshore equities market, there is reason to extend coverage to mid caps, which represented approximately USD 1.6 trillion in total market cap as of April 29, 2022. In fact, while large-cap China A-shares represented the largest market after the U.S., the market cap of the S&P China A MidCap 500 Index was nearly the size of Australia and was larger than several established markets including Hong Kong, Sweden, the Netherlands and Brazil, among others.

Exhibit 1: Mid-Cap China A-Shares Are Larger than Many Domestic Markets



Source: S&P Dow Jones Indices LLC. Data as of April 29, 2022. Chart is provided for illustrative purposes. Chart excludes the U.S. (USD 44,479 billion total market cap) to aid visualization.

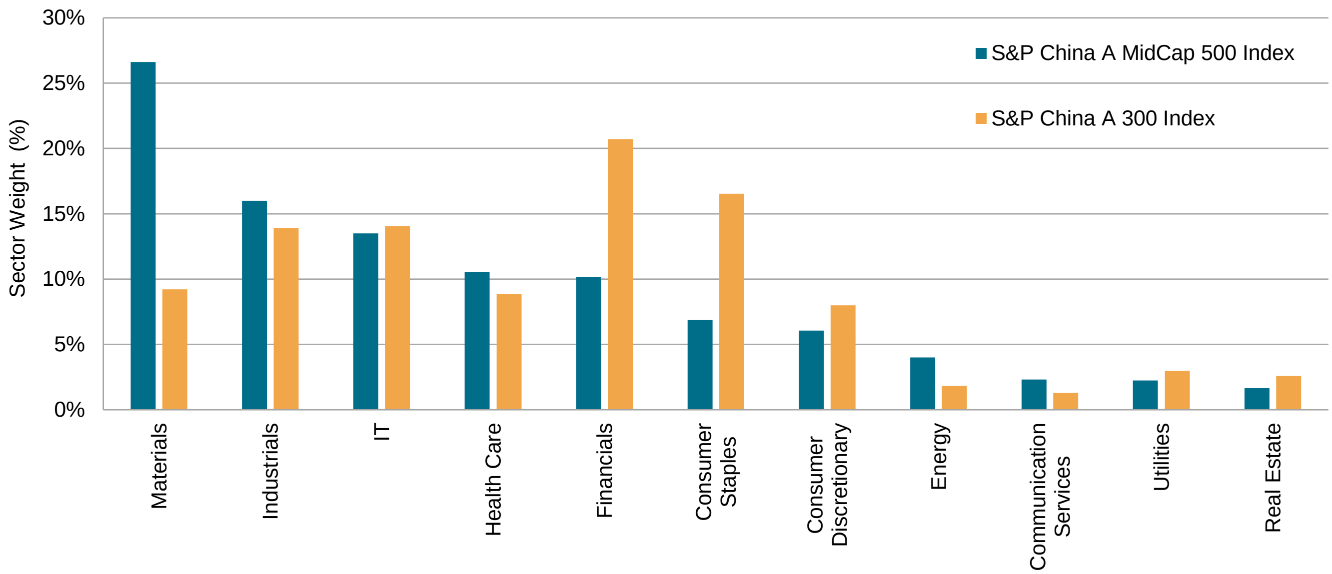
An Overview of the S&P China A Midcap 500 Index

The S&P China A MidCap 500 Index uses a simple, rules-based methodology to select 500 of the largest and most-liquid Chinese companies that follow in size after companies in the S&P China A 300 Index. The eligible universe includes all Chinese companies that meet positive earnings per share (EPS) requirements over the two most recent trailing 12-month periods and minimum liquidity thresholds. The index selection process reflects GICS® sector balance considerations and is rebalanced semiannually in June and December.[1]

Considerations for Mid-Cap A-Share Sector Exposure

The sector composition of the S&P China A MidCap 500 Index varies widely from the more traditional sector exposure found in the S&P China A 300 Index. While Financials and Consumer Staples sectors represented over 35% of the S&P China A 300 Index as of April 29, 2022, the S&P China A MidCap 500 Index was most heavily weighted to Materials, Industrial and Information Technology (see Exhibit 2).

Exhibit 2: Sector Exposure of the S&P China A MidCap 500 Index versus S&P China A 300 Index



Source: S&P Dow Jones Indices LLC. Data as of April 29, 2022. Chart is provided for illustrative purposes.

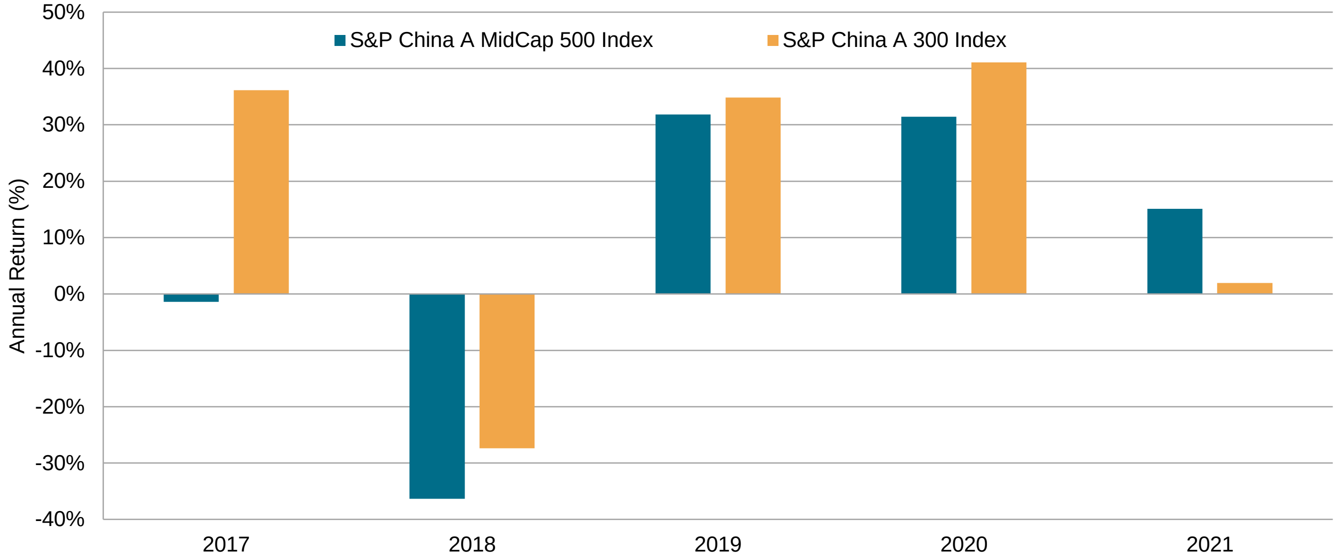
The returns dispersion between the S&P China A MidCap 500 Index and S&P China A 300 Index illustrates the differentiated exposure between the two size classes (see Exhibit 3). In fact, the average variance in performance over the past five calendar years was 9.2%, and large caps beat mid caps by nearly 40% in 2017.

In 2021, several factors affected returns, as greater relative Materials and Industrials exposure drove the outperformance of the mid-cap segment. Conversely, in 2017, most large-cap

[1] For a more complete overview of methodology details, see the Appendix and the S&P China Indices Methodology.

sectors outperformed their mid-cap counterparts, while Information Technology companies, which were more prevalent in the large-cap index, led the outperformance.

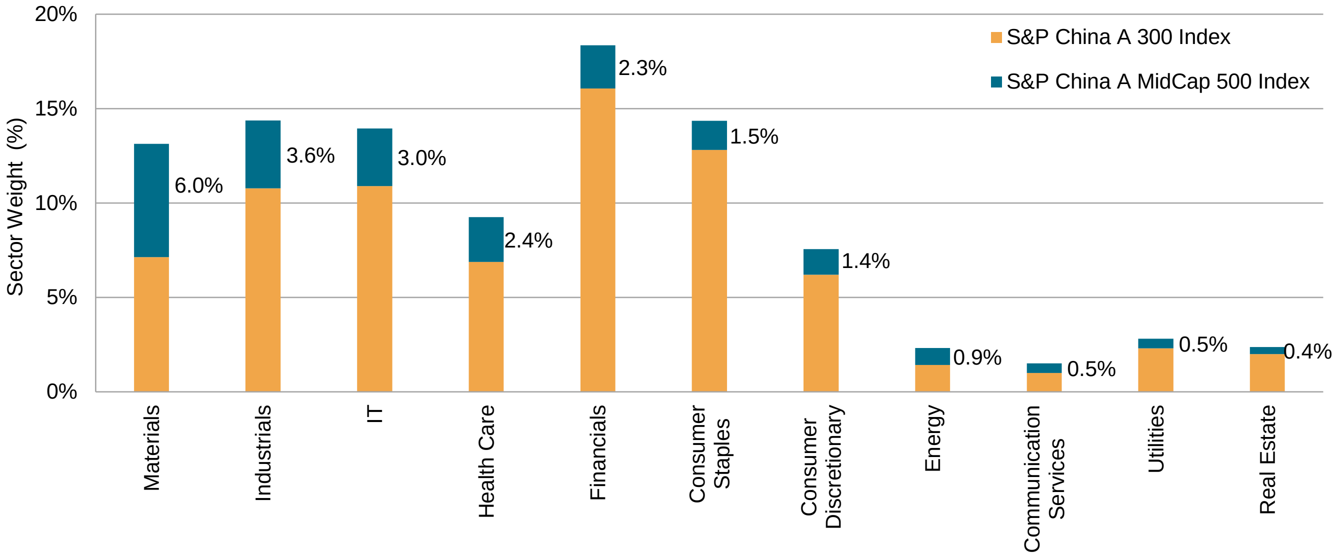
Exhibit 3: High Return Dispersion between Mid-Cap and Large-Cap A-Shares



Source: S&P Dow Jones Indices LLC. Data as of April 29, 2022. Index performance based on USD in total return. Past performance is no guarantee of future results. The S&P China A MidCap 500 Index was launched Aug. 17, 2020. All data prior to index launch date is back-tested hypothetical data. Chart is provided for illustrative purposes and reflects hypothetical historical performance. Please see the Performance Disclosure at the end of this document for more information regarding the inherent limitations associated with back-tested performance.

Combining the S&P China A 300 Index and S&P China A MidCap 500 Index resulted in a more even distribution across sectors. A review of a combined large- and mid-cap exposure showed that the mid-cap additions had the greatest impact on Materials, Industrials and Information Technology weight, while the addition of mid caps did little to augment weight in Real Estate, Utilities and Communication Services (see Exhibit 4).

Exhibit 4: Mid-Cap A-Shares Could Complement Exposure in Key Sectors



Source: S&P Dow Jones Indices LLC. Data as of April 29, 2022. Chart is provided for illustrative purposes.

Key Characteristics of the S&P China A MidCap 500 Index

While the S&P China A 300 Index is designed to provide sufficient exposure to traditional large-cap China A-Shares, the S&P China A MidCap 500 Index offers unique advantages for market participants seeking a more comprehensive China A exposure inclusive of mid-cap A-shares.

Profitability Screen. The requirement for positive earnings provides reassurance that less-established mid caps that lack a track record of generating positive earnings are excluded from the index.

Exclusion of Sanctioned Securities. The S&P China A MidCap 500 Index is maintained from a U.S./U.K./EU perspective and therefore excludes securities sanctioned by governments in these jurisdictions, including those affected by U.S. Executive Orders 13959 and 14032. This could provide an advantage to those who may otherwise be unnecessarily exposed to tracking error if following an index that includes sanctioned securities.

Differentiated Exposures Demonstrated by Historical Performance Profiles. The S&P China A MidCap 500 Index posted lower risk-adjusted performance over the periods studied, an indication of the differentiated exposures offered by the two indices (see Exhibit 5).

Exhibit 5: Comparison of Historical Performance

Period	S&P China A MidCap 500 Index	S&P China A 300 Index
Annualized Returns (%)		
1-Year	-16.81	-20.44
3-Year	2.36	4.89
5-Year	-1.75	7.27
10-Year	3.38	7.01
Standard Deviation (%)		
3-Year	21.76	19.86
5-Year	22.79	19.86
10-Year	28.07	23.39
Risk-Adjusted Return		
3-Year	0.11	0.25
5-Year	-0.08	0.37
10-Year	0.12	0.30

Source: S&P Dow Jones Indices LLC, FactSet. Data as of April. 29, 2022. Index performance based on total return in USD. The S&P China A MidCap 500 Index was launched Aug. 17, 2020. All data prior to index launch date is back-tested hypothetical data. Table is provided for illustrative purposes and reflects hypothetical historical performance. Please see the Performance Disclosure at the end of this document for more information regarding the inherent limitations associated with back-tested performance..

Conclusion

The S&P China A MidCap 500 Index seeks to measure mid-cap onshore Chinese equities, enabling market participants to expand beyond the limited coverage offered by large-cap indices. Mid caps provide differentiated sector exposure and when paired with large caps, could offer greater breadth of coverage. Unique advantages of the S&P China A MidCap 500 Index, when compared to other established onshore mid-cap-focused China benchmarks, include profitability and sector balance criteria, and the exclusion of sanctioned companies.

Appendix

About the S&P China A MidCap 500 Index

The S&P China A MidCap 500 Index is designed to measure the performance of the mid-cap segment of the China A-shares universe that is traded on the Shenzhen or Shanghai exchange.

Index Methodology Overview

Inclusion Requirements

1. Constituents must be included in the S&P China A 1800 Index.

2. Stocks with negative EPS for the two most recent trailing 12-month periods are ineligible for index inclusion.

3. Stocks must be ranked in the top 85% of the index universe by six-month median daily value traded (top 90% for current constituents).

Constituent Selection

1. S&P China A 300 Index constituents are ineligible for index inclusion. Remaining eligible stocks are ranked in descending order by total market capitalization.

2. The top 500 eligible stocks ranked by total market capitalization are selected, subject to current constituents remaining in the index if they rank among the top 750 stocks.

Weighting

The index is weighted by float-adjusted market cap. The investable weight factor for the stocks in the index reflect the percentage of shares available to Chinese mainland investors.

Rebalancing

The index is rebalanced semiannually, effective after the close of trading on the third Friday of June and December. The rebalancing reference dates are the third Friday of May and November, respectively.

Investor Perspective

The S&P China A MidCap 500 Index is maintained from a U.S./U.K./EU investor perspective and therefore excludes securities sanctioned by governments in these jurisdictions including those affected by U.S. Executive Orders 13959 and 14032.

Performance Disclosure/Back-Tested Data

The S&P China A MidCap 500 Index was launched August 17, 2020. All information presented prior to an index's Launch Date is hypothetical (back-tested), not actual performance. The back-test calculations are based on the same methodology that was in effect on the index Launch Date. However, when creating back-tested history for periods of market anomalies or other periods that do not reflect the general current market environment, index methodology rules may be relaxed to capture a large enough universe of securities to simulate the target market the index is designed to measure or strategy the index is designed to capture. For example, market capitalization and liquidity thresholds may be reduced. Complete index methodology details are available at www.spglobal.com/spdji. Past performance of the Index is not an indication of future results. Back-tested performance reflects application of an index methodology and selection of index constituents with the benefit of hindsight and knowledge of factors that may have positively affected its performance, cannot account for all financial risk that may affect results and may be considered to reflect survivor/look ahead bias. Actual returns may differ significantly from, and be lower than, back-tested returns. Past performance is not an indication or guarantee of future results. Please refer to the methodology for the Index for more details about the index, including the manner in which it is rebalanced, the timing of such rebalancing, criteria for additions and deletions, as well as all index calculations. Back-tested performance is for use with institutions only; not for use with retail investors.

S&P Dow Jones Indices defines various dates to assist our clients in providing transparency. The First Value Date is the first day for which there is a calculated value (either live or back-tested) for a given index. The Base Date is the date at which the index is set to a fixed value for calculation purposes. The Launch Date designates the date when the values of an index are first considered live: index values provided for any date or time period prior to the index's Launch Date are considered back-tested. S&P Dow Jones Indices defines the Launch Date as the date by which the values of an index are known to have been released to the public, for example via the company's public website or its data feed to external parties. For Dow Jones-branded indices introduced prior to May 31, 2013, the Launch Date (which prior to May 31, 2013, was termed "Date of introduction") is set at a date upon which no further changes were permitted to be made to the index methodology, but that may have been prior to the Index's public release date.

Typically, when S&P DJI creates back-tested index data, S&P DJI uses actual historical constituent-level data (e.g., historical price, market capitalization, and corporate action data) in its calculations. As ESG investing is still in early stages of development, certain datapoints used to calculate S&P DJI's ESG indices may not be available for the entire desired period of back-tested history. The same data availability issue could be true for other indices as well. In cases when actual data is not available for all relevant historical periods, S&P DJI may employ a process of using "Backward Data Assumption" (or pulling back) of ESG data for the calculation of back-tested historical performance. "Backward Data Assumption" is a process that applies the earliest actual live data point available for an index constituent company to all prior historical instances in the index performance. For example, Backward Data Assumption inherently assumes that companies currently not involved in a specific business activity (also known as "product involvement") were never involved historically and similarly also assumes that companies currently involved in a specific business activity were involved historically too. The Backward Data Assumption allows the hypothetical back-test to be extended over more historical years than would be feasible using only actual data. For more information on "Backward Data Assumption" please refer to the FAQ. The methodology and factsheets of any index that employs backward assumption in the back-tested history will explicitly state so. The methodology will include an Appendix with a table setting forth the specific data points and relevant time period for which backward projected data was used.

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