

# FTSE BURSA MALAYSIA INDEX SERIES

## Enhanced Median Liquidity Rule Overview - December 2011

### Introduction

The FTSE Bursa Malaysia Index Series at the December 2011 index review will be changing the way it screens companies for liquidity. The following paper provides an overview of why companies are screened for liquidity. It looks at the existing index series liquidity screen, and demonstrates that an enhanced median liquidity rule, that will be applied to the companies in the FTSE Bursa Malaysia Index Series from December 2011, will provide a more accurate representation of true company investability.

### Importance of Liquidity Screened Indices

The primary objective of a benchmark index should be to achieve an accurate representation of the investable universe. Including companies without a minimum level of liquidity will impact the usefulness of an index:

- A company might have the best share price performance but inability to trade it could reflect poorly on a fund manager benchmarked to the index
- A company might only trade around the reporting season causing investment issues if traded at any other time
- Less liquid companies will generally cost more to trade, but also depending on the size of the trade impact the share price, and cause capacity issues to the fund

### FTSE Bursa Malaysia Index Series old liquidity rule overview (Pre-December 2011)

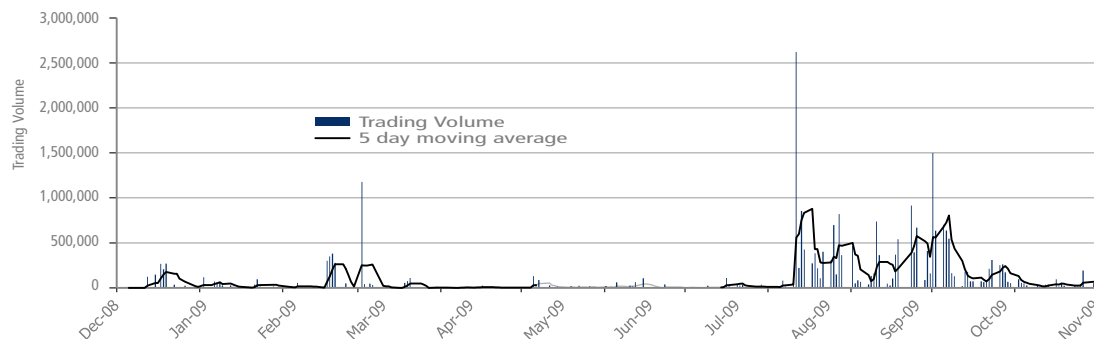
The existing FTSE Bursa Malaysia Index Series liquidity rule removes companies which do not turnover at least 10% of their free float adjusted shares, in the twelve months prior a semi-annual review.

$$\frac{\text{12 month share volume}}{\text{Free float adjusted shares}} = x\%$$

The liquidity rule has provided a means of screening out companies that are not sufficiently liquid, however, feedback from investors has shown there is room for improvement.

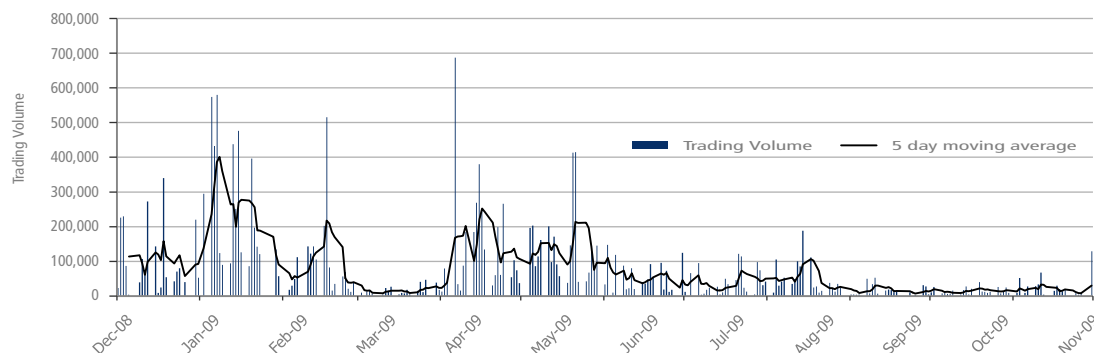
The below example illustrates limitations of the old liquidity rule. Company A and Company B, both have a similar market capitalisation, and passed the existing liquidity rule with a percentage of over 30%.

#### Example : Company A



By comparing the liquidity patterns of two similar sized companies, we can see that Company B trades more consistently compared to Company A

#### Example : Company B



The existing liquidity rule does not differentiate between the trading pattern of company A and B

The old liquidity rule does not differentiate between companies that trade regularly and those that trade irregularly. Company A did not trade for 56 days over the 1 year period. Although the volume for Company B is volatile, there is a more consistent number of shares trading on a daily basis. An investor would prefer to trade Company B.

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# FTSE BURSA MALAYSIA INDEX SERIES

## Enhanced Median Liquidity Rule Overview - December 2011

### Enhanced FTSE Bursa Malaysia Index Series median liquidity rule overview

The enhanced median liquidity rule has been developed in conjunction with the FTSE Global Index Committees, consisting of leading market professionals from around the globe, including plan sponsors, consultants, investment managers and financial analysts.

The enhanced median liquidity rule provides a more accurate representation of true investability, which is used by FTSE and other international index providers to screen out illiquid companies. The liquidity rule aligns the series to global standards whilst continuing to provide an accurate representation of the true investability of companies in the FTSE Bursa Malaysia Index Series.

The median liquidity enhancement aligns the series to global standards

Companies are tested for liquidity at the June and December reviews using daily volume data on a month-by-month basis, over a 12 month period

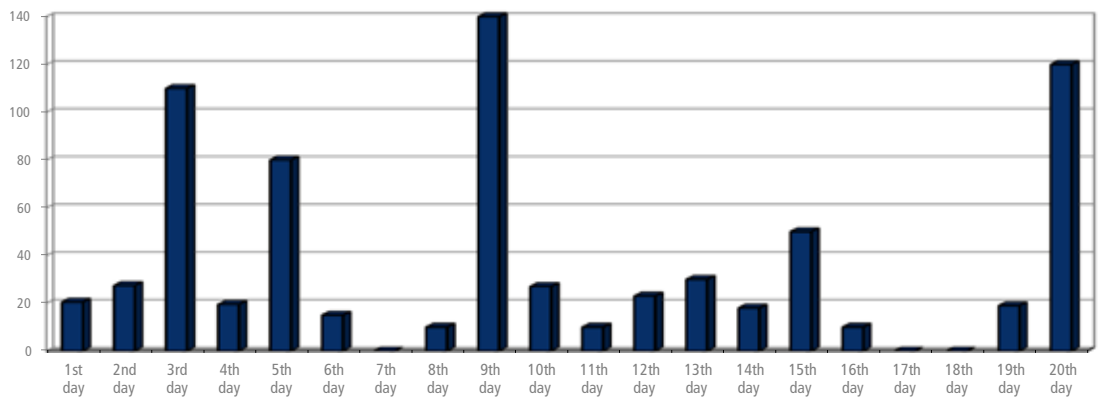
#### Sufficiently liquid companies must:

- Pass a **0.04%** median liquidity threshold for **8 out of 12 months** of the year for **existing constituents**
- Pass a **0.05%** median liquidity threshold for **10 out of 12 months** of the year for **index additions**

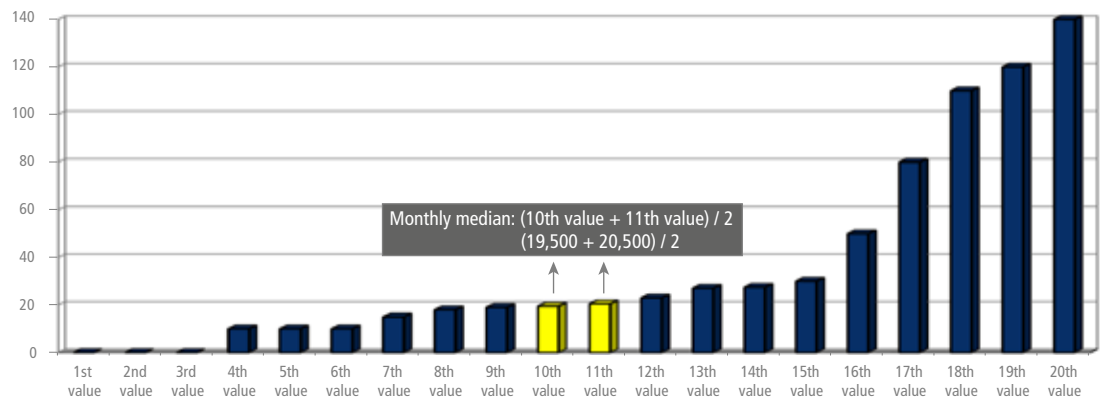
Companies will be tested for liquidity on a semi-annual basis in June and December as part of the FTSE Bursa Malaysia Index Series index review.

#### Example: Application of the enhanced liquidity rule

For each month, the daily trading of Company C is analysed



For each month, FTSE ranks the daily volumes and selects the median value



#### Monthly median liquidity calculation for Company C

Monthly median of daily volumes / free float adjusted shares

$$20,000 / 400,000 = 0.05\%$$

A company that trades a 0.05% median liquidity number is equivalent to trading 1% of its value in a month (1% / 20 trading days per month)

Companies are tested for liquidity using daily volume data on a month-by-month basis, over a 12 month period prior to the index review.

# FTSE BURSA MALAYSIA INDEX SERIES

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For each month a monthly median percentage value is created. Each value is then screened according to the particular rule for either an existing index constituent or non-constituent.

As an example, at the current December 2011 index review of the FTSE Bursa Malaysia KLCI, MISC will be removed from the index as it has failed the 0.04% median liquidity threshold. It's median liquidity values on a monthly basis are provided in the table below along with the company that will be replacing it in the FTSE Bursa Malaysia KLCI.

### Analysis of FTSE Bursa Malaysia KLCI constituents' median liquidity result:

MISC does not pass the enhanced median liquidity rule, and will be removed from the FTSE Bursa Malaysia KLCI at the December 2011 index review

AirAsia passes the enhanced median liquidity rule, and will replace MISC in the FTSE Bursa Malaysia KLCI at the December 2011 index review

MISC			
Month	Median Liquidity	Pass / Fail	Number of Passes
December 2010	0.056%	✓	1
January 2011	0.049%	✓	2
February 2011	0.066%	✓	3
March 2011	0.040%	✓	4
April 2011	0.021%	✗	
May 2011	0.043%	✓	5
June 2011	0.037%	✗	
July 2011	0.035%	✗	
August 2011	0.045%	✓	6
September 2011	0.048%	✓	7
October 2011	0.031%	✗	
November 2011	0.026%	✗	

AirAsia			
Month	Median Liquidity	Pass / Fail	Number of Passes
December 2010	0.283%	✓	1
January 2011	0.502%	✓	2
February 2011	0.549%	✓	3
March 2011	0.383%	✓	4
April 2011	0.369%	✓	5
May 2011	0.369%	✓	6
June 2011	0.242%	✓	7
July 2011	0.342%	✓	8
August 2011	0.866%	✓	9
September 2011	0.630%	✓	10
October 2011	0.677%	✓	11
November 2011	0.677%	✓	12

The following table highlights the indices that are screened for liquidity using the enhanced median liquidity rule:

Liquidity tested	Not liquidity tested
FTSE Bursa Malaysia KLCI	FTSE Bursa Malaysia Fledgling Index
FTSE Bursa Malaysia Mid 70 Index	FTSE Bursa Malaysia ACE Index
FTSE Bursa Malaysia Top 100 Index	
FTSE Bursa Malaysia Small Cap Index	
FTSE Bursa Malaysia EMAS Index	
FTSE Bursa Malaysia EMAS Industry Indices	
FTSE Bursa Malaysia EMAS Shariah Index	
FTSE Bursa Malaysia Hijrah Shariah Index	
FTSE Bursa Malaysia Palm Oil Plantation Index	
FTSE Bursa Malaysia Asian Palm Oil Plantation Index	



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