
INDICES FOR BEGINNERS

WHAT IS AN INDEX?

An index is a statistical measure of the changes in a portfolio of stocks representing a portion of the overall market. This number summarises the fluctuation of share prices on a given day. An index's primary purpose is to reflect the aggregate movement of the market it represents. Hence, a single index value would be meaningless if not compared to a previous/historical value.

HOW ARE INDICES CALCULATED?

The FTSE Group and the JSE entered into a partnership to create the FTSE/JSE Africa Index Series in 2002. The series brought about a change in the philosophy and methodology for calculating indices and classifying sectors. The main feature was the move from indices based on full market capitalisation, to free float-adjusted indices. Free float is the number of shares freely available to investors. It excludes those shares where shareholding is restricted to specific individuals or groups of individuals.

FTSE/JSE calculates both a capital and a total return for all indices, where the capital index is the summation of the market values (or capitalisations) of all companies within the index.

The Total Returns Indices (TRIs) measure the total return on the underlying indices, combining both capital performance and reinvested income. The TRIs are calculated using declared dividends.

CALCULATION METHODOLOGY

- Determine the universe and those instruments that are eligible, depending on the index being created
- Set the rules for constituent addition and deletion
- Add the free floated market capitalisation of all the constituents
- Set the index starting value at 100
- Determine the divisor.

$$\text{INDEX VALUE} = \frac{\text{Sum of Free Float Market Capitalisation of All Constituent Companies}}{\text{Latest Index Divisor}}$$

- The free float market capitalisation of each company is calculated by multiplying the most recent share price by the number of shares after the free float weighting has been applied
- The index divisor is an arbitrary number chosen at the starting point of the index, which is adjusted when capitalisation amendments are made to the constituents of the index allowing the index value to remain comparable over time.

HOW ARE INDICES USED?

Indices can be used as a benchmark in the way that the All Share index (Alsi) is used in our market. In this way it acts as a proxy for the performance of all companies listed on the JSE. Indices can also be used to measure performance, for instance, one can use the bank's index to measure the performance of the banking sector.

Because indices are calculated from different base values, the percentage change is more important than the actual numeric value. Technically, one can't actually invest in an index. But one can invest in products like Exchange Traded Funds (ETFs) or derivatives which are based on these indices.

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DIFFERENT TYPES OF INDICES

The FTSE/JSE Africa Index Series may be roughly grouped into the categories listed below:

- **Headline** – used for benchmarking, eg All Share index
- **Tradable** – used for trading and funds, eg Top 40 index
- **Secondary market indices**, eg AltX index
- **Specialist indices** – special features, eg Dividend+ index
- **Sector and economic group indices** – measures the performance of a particular industry or sector, eg bank's index
- **Custom indices** – custom built for specific clients, eg Absa New Rand index used for their ETF.

A number of indices have been added to the series over the years:

Capi

- Follows the structure of the FTSE/JSE All Share index in terms of constituents, data and application of corporate actions
- All constituents with a weighting larger than 10% in the index will be capped at a fixed level of 10%.

Swix

- Follows the structure of the FTSE/JSE All Share

index in terms of constituents, but certain constituents' weights are adjusted for non-South African shareholding.

Style

- Style can be defined as an investment strategy that groups companies by different rates of return. Methodology determines a value and growth ranking for each company.

Dividend+

- Yield-weighted index is designed to measure the performance of high-yielding shares. Index selects the top 30 shares by one-year forecast dividend from the FTSE/JSE Top 40 and Mid Cap indices, excluding real-estate companies.

Shariah

- Represents the performance of Shariah compliant companies from the FTSE/JSE All Share index
- FTSE's Shariah compliant constituents are screened by Yasaar Research Inc, an independent Shariah screening company.

RAFI 40

- Top 40 companies ranked on specific factors – book value, cash flow, sales and dividend
- Methodology developed by Research Affiliates in the US, designed to reflect the top 40 companies

from the FTSE/JSE Africa All Share Index by fundamentals

- The constituents may differ from the constituents in the FTSE/JSE Top 40.

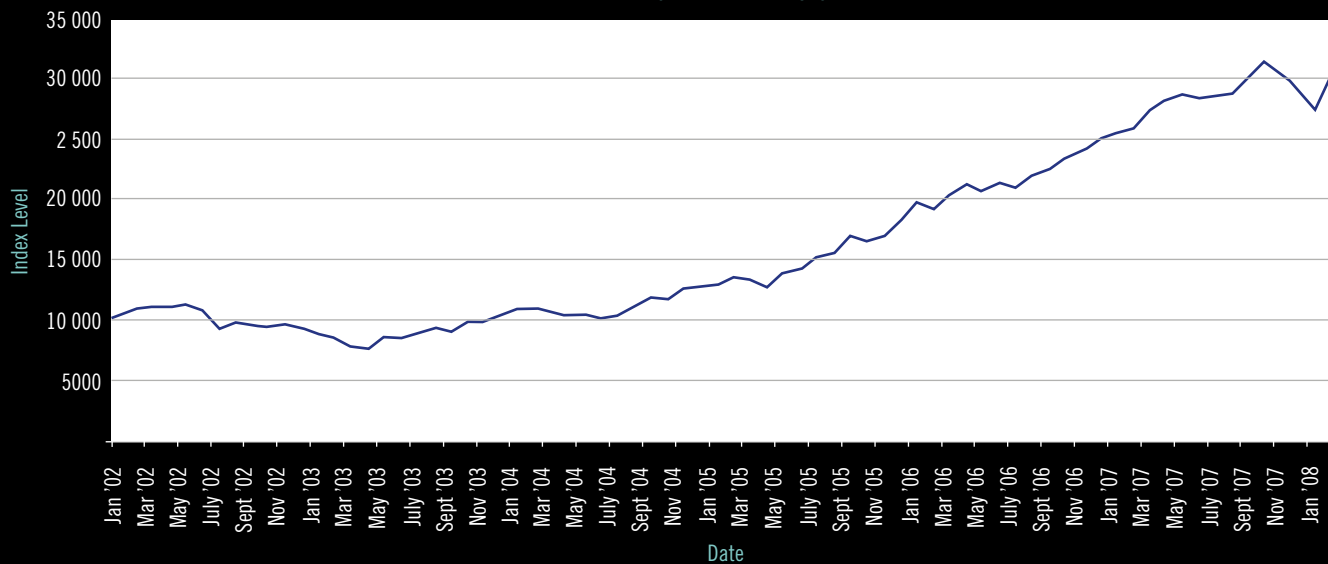
REVIEW OF INDICES

The majority constituents of the FTSE/JSE Africa Index Series are reviewed quarterly, in March, June, September, and December in accordance with the FTSE/JSE Africa Index Series ground rules. Insertion and deletion of constituents of the indices is not restricted to the quarterly review and may be done at any time that a corporate event occurs which would impact the indices.

The rules for inserting and deleting companies at the quarterly review are designed to provide stability in the selection of constituents of the FTSE/JSE Africa Index Series while ensuring that the indices continue to be representative of the market by including or excluding those companies which have risen or fallen significantly.

Below is the performance of the FTSE/JSE All Share index.

ALL SHARE INDEX VALUES



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