

# **Indxx SuperDividend® U.S. Low Volatility Index**

## **Methodology**

**May 2015**

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# Indxx SuperDividend® U.S. Low Volatility Index

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## Index Description

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The Indxx SuperDividend® U.S. Low Volatility Index is a 50-stock equal weighted index designed to measure the market performance of companies in the United States that have a high dividend yield and low beta. The index was incorporated on February 29, 2008.

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## Selection Pool

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### ***Market Capitalization***

Minimum market capitalization is set at US\$ 500 million

### ***Liquidity***

- Minimum average daily turnover for 6 months has been set at US\$ 1 million
- The stock should have traded for at least 90% of the total trading days over the last 6 months in its respective stock exchange

### ***Domicile***

A US company, for index purposes, should have the following characteristics:

- Domiciled in the US
- Listed on any of the US stock exchanges

### ***Public Float***

Public float or free float should be at least 10% of the total shares outstanding for each member

### ***Beta***

Beta of each constituent with respect to its local country benchmark, should be less than or equal to 0.85

### ***Dividend Yield***

Trailing 12 month dividend yield of all constituents should be in the range of 1% - 20%. Each constituent should have paid dividends consistently for the last 2 years and the current year dividend should be greater than or equal to 50% of the previous year.

### ***Security Type***

Common Stocks, Master Limited Partnership and REITs

BDCs will not be considered for inclusion in the portfolio

### ***Weighting***

All constituents in the portfolios are equally weighted. Additionally, no one particular sector can have a weight greater than 25% and MLPs should not constitute more than 20% of the index.

### ***Annual Reconstitution***

1. Portfolio will be reconstituted once a year on the last business day in February (reconstitution day). On the selection day (third last Friday of February each year), a new selection pool will be created.
2. All the existing index constituents, which appear in the top 200 companies, ranked by dividend yield in the selection pool (top 200), will be retained.
3. Existing index constituents that are not part of the top 200 are replaced by the companies with the largest dividend yield in the top 200, subject to sector and security cap.
4. Dividend forecast for selected constituents should be stable, i.e. there should be no official announcement as of the selection day, that dividend payments are likely to be cancelled or significantly reduced in the future.

### ***Quarter Rebalance***

Apart from the reconstitution, at the end of every quarter (five business days before the last trading day in May, August and November), the index components are screened for dividend cuts or an overall negative outlook concerning the companies' dividend policy. A Company excluded during these quarterly reviews will be replaced by a company in the top 200 that is currently not an index member. This company will be given the same weight as the company that is deleted, calculated as on the trading day before the rebalancing takes place. In case more than one company is deleted, the cumulative weight of the companies is calculated and distributed equally among the replacements.

## Index Creation Process

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A master list of the securities is initially prepared from the applicable Index Universe by applying the criteria of market capitalization and beta. All companies with (i) market capitalization below US\$ 500 million and (ii) a beta of more than 0.85 are eliminated. The remaining companies are screened for turnover and companies with a 6-month average daily turnover of less than US\$ 1 million are eliminated. Thereafter, the dividend yield for the remaining companies is calculated. All companies with dividend yields below 1% or above 20% are then removed to obtain a 'Selection List'.

The Selection List is ranked according to dividend yield and checked for dividend consistency in the last 2 years. Companies which do not display consistent dividends are removed and public float for the remaining companies is checked. Companies, which do not have at least 10% of public float, are removed to arrive at the 'Selection pool'.

The selection pool is ranked by dividend yield and top 200 companies are selected. To determine the initial composition, the companies in the selection pool are ranked in descending order according to their dividend yield. The 50 companies with the largest dividend yield on that day are chosen as index constituents. All constituents in the portfolios are equally weighted. Additionally, no one particular sector can have a weight greater than 25% and MLPs should not constitute more than 20% of the index. On the annual reconstitution day, existing index constituents, which are not part of the top 200 companies, will be replaced by the company with the largest dividend yield that is currently not an index member, subject to sector and security cap.

# Corporate Actions

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Corporate actions (such as stock splits, dividends, spin-offs and rights offerings) are applied on the ex-date. The impact and adjustment of various corporate actions are discussed below.

## Dividends

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### Meaning

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Dividends are payments made by a corporation to its shareholder members. It is the portion of corporate profits paid out to stockholders. When a corporation earns a profit or surplus, that money can be put to two uses: it can either be re-invested in the business (called retained earnings), or it can be paid to the shareholders as a dividend. Many corporations retain a portion of their earnings and pay the remainder as a dividend.

Dividends must be "declared" (approved) by a company's Board of Directors each time they are paid. For public companies, there are four important dates to remember regarding dividends.

1. **Declaration Date:** Is the day the Board of Directors announces its intention to pay a dividend. On the declaration date, the Board will also announce Date of Record and Payment Date.
2. **In-dividend Date:** Is the last day, which is one trading day before the ex-dividend date, where the stock is said to be cum dividend ('with dividend').
3. **Ex-dividend Date:** Is the day on which all shares bought and sold no longer come attached with the right to be paid the most recently declared dividend. Typically, its 2 trading days before the record date for U.S. securities.
4. **Payment Date:** Is the day when the dividend checks will actually be mailed to the shareholders of a company or credited to brokerage accounts.

### Impact on Index

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Dividends payments impact the total return index calculation. The price return index calculations as well as the number of shares remain unaffected.

### Adjustment in the Index

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Dividend payments will be reinvested in the total return index on the ex-dividend date. This means that going forward this additional money will be used to buy additional shares in the future.

## Stock Split

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### Meaning

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All publicly-traded companies have a set number of shares that are outstanding on the stock market. A stock split is a decision by the company's board of directors to increase the number of shares that are outstanding by issuing more shares to current shareholders. For example, in a 2-for-1 stock split, every shareholder with one stock is given an additional share. So, if a company had 10 million shares outstanding before the split, it will have 20 million shares outstanding after a 2-for-1 split.

A stock's price is also affected by a stock split. After a split, the stock price will be reduced since the number of shares outstanding has increased. In the example of a 2-for-1 split, the share price will be halved. Thus, although the number of outstanding shares and the stock price change, the market capitalization remains constant. A stock split is usually done by companies that have seen their share price increase to levels that are either too high or are beyond the price levels of similar companies in their sector. The primary motive is to make shares seem more affordable to small investors even though the underlying value of the company has not changed.

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### Impact on Index

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Stock splits impact the number of shares in both the total and price return indices. There is no impact on the index divisor.

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### Adjustment in the Index

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Stock splits will be adjusted for in the total and price return indices on the ex- date. The number of shares will increase times the adjustment factor for the split. For example if a company has announced a 2-for-1 stock split, the adjustment factor for the same will be  $2/1=2$ . The number of shares in this case will be multiplied by 2.

## Bonus Issue of Shares

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### Meaning

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A bonus share is a free share of stock given to current/existing shareholders in a company, based upon the number of shares that the shareholder already owns at the time of announcement of the bonus. While the issue of bonus shares increases the total number of shares issued and owned, it does not increase the value of the company. Although the total number of issued shares increases, the ratio of number of shares held by each shareholder remains constant. New shares are issued to shareholders in proportion to their holdings. For example, the company may give one bonus share for every five shares held.

### Impact on Index

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Bonus issue of shares impacts the number of shares in both the total and price return indices. There is no impact on the index divisor.

### Adjustment in the Index

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Bonus issue of shares will be adjusted for in the total and price return indices on the ex- date. The number of shares will increase times the adjustment factor for the bonus issue. For example if a company has announced a 100% bonus, the adjustment factor for the same will be 2 i.e. one bonus share for every one share held. The number of shares in this case will be multiplied by 2.



## **Rights Issue**

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### **Meaning**

Rights issue is an invitation to existing shareholders to purchase additional new shares in the company. More specifically, this type of issue gives existing shareholders securities called "rights", which, will, give the shareholders the right to purchase new shares at a discount to the market price on a stated future date. The company is giving shareholders a chance to increase their exposure to the stock at a discount price. But until the date at which the new shares can be purchased, shareholders may trade the rights on the market the same way they would trade ordinary shares. The rights issued to a shareholder have a value, thus compensating current shareholders for the future dilution of their existing shares' value.

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### **Impact on Index**

Rights issue impacts the number of shares in both the total and price return indices. There will be an impact on the divisors in both the total and price return indices.

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### **Adjustment in the Index**

Rights issue will be adjusted for in the total and price return indices on the ex- date. However the adjustment for rights issue will take place only when the subscription price is less than the stock price on ex-date. The subscription price is the price at which the company gives its existing shareholders the right to purchase new shares.

## Spin Off

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### Meaning

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Spin off is the creation of an independent company through the sale or distribution of new shares of an existing business/division of a parent company. A spinoff is a type of divestiture. Businesses wishing to 'streamline' their operations often sell less productive or unrelated subsidiary businesses as spinoffs. The spun-off companies are expected to be worth more as independent entities than as parts of a larger business.

In most cases, the parent company or organization offers support doing one or more of the following:

- Investing equity in the new firm,
- Being the first customer of the spin-out (helps to create cash flow),
- Providing incubation space (desk, chairs, phones, internet access, etc.) or
- Providing services such as legal, finance, technology, etc.

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### Impact on Index

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Spin off impacts the divisors in both the total and price return indices.

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### Adjustment in the Index

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The adjustment for spin off is done on a case to case basis. The Index Committee will decide on one of the following options based on internal research:

- The parent company remains in the index and the spun off entity is deemed ineligible for inclusion
- The parent company is deemed ineligible to remain in the index however, the spun off entity is deemed eligible for inclusion
- Neither the parent company nor the spun off entity are eligible to be in the index. In this case the Index Committee will decide whether to liquidate the parent company in the index or replace it with the next best constituent according to the index methodology

## Delisting

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### Meaning

Delisting refers to the practice of removing the stock of a company from a stock exchange so that investors can no longer trade shares of the stock on that exchange. This typically occurs when a company goes out of business, declares bankruptcy, no longer satisfies the listing rules of stock exchange, or has become a private company after a merger or acquisition, or wants to reduce regulatory reporting complexities and overhead, or if the stock volumes on the exchange from which it wishes to delist are not significant.

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### Impact on Index

Delisting of a security impacts the divisors in both the total and price return indices.

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### Adjustment in the Index

In the event a company is de-listed from the listed exchange, it will be removed from the index. The Index Committee will decide whether to liquidate the stock in the index or to replace it with the next best constituent according to the index methodology.

## Acquisition

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### Meaning

A corporate action in which a company buys most, if not all, of the target company's ownership stakes in order to assume control of the target firm. Acquisitions are often made as part of a company's growth strategy whereby it is more beneficial to take over an existing firm's operations and niche compared to expanding on its own. Acquisitions are often paid in cash, the acquiring company's stock or a combination of both. Acquisitions can be either friendly or hostile.

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### Impact on Index

Acquisition of a security impacts the divisors in both the total and price return indices.

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### Adjustment in the Index

In the event a company is acquired, it will be removed from the index. The Index Committee will decide whether to liquidate the stock in the index or to replace it with the next best constituent according to the index methodology.

## Merger

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### Meaning

Merger is when two companies combine together to form a new company altogether. In other words, it is the combination of two or more companies, generally by offering the stockholders of one company securities in the acquiring company in exchange for the surrender of their stock.

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### Impact on Index

Merger impacts the divisors in both the total and price return indices.

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### Adjustment in the Index

In the event a company is merged, it will be removed from the index. The Index Committee will decide whether to liquidate the stock in the index or to replace it with the next best constituent according to the index methodology.

## **Bankruptcy**

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### **Meaning**

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Bankruptcy is a legal proceeding involving a person or business that is unable to repay outstanding debts. The bankruptcy process begins with a petition filed by the debtor (most common) or on behalf of creditors (less common). All of the debtor's assets are measured and evaluated, whereupon the assets are used to repay a portion of outstanding debt. Upon the successful completion of bankruptcy proceedings, the debtor is relieved of the debt obligations incurred prior to filing for bankruptcy.

### **Impact on Index**

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Bankruptcy of a security impacts the divisors in both the total and price return indices.

### **Adjustment in the Index**

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In the event a company is Bankrupt, it will be removed from the index. The Index Committee will decide whether to liquidate the stock in the index or to replace it with the next best constituent according to the index methodology.

## Temporary Delisting/Prolonged Trading Suspension

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### Meaning

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A temporary delisting/trading suspension occurs when a security stops trading on the stock exchange for a certain time period. This usually occurs when a publicly-traded company is going to release significant news about itself. The suspension in trading for the affected security gives investors time to review the news and assess its impact.

### Impact on Index

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A temporary delisting/trading suspension of a security impacts the divisors in both the total and price return indices.

### Adjustment in the Index

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In the event a company is temporary delisted or trading suspension has taken place, it will be removed from the index. The Index Committee will decide whether to liquidate the stock in the index or to replace it with the next best constituent according to the index methodology.

## Index Data

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### **Total Return Index**

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Ordinary cash dividends are applied on the ex-date for calculating the total return index. "Special dividends" are those dividends that are outside of the normal payment pattern established historically by the issuing corporation. Whether a dividend is funded from operating earnings or from other sources of cash does not affect the determination of whether it is ordinary or special. "Special dividends" are treated as corporate actions with offsetting price and divisor adjustments; the total return index reflects both ordinary and special dividends.

### **Price Return Index**

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No dividends are applied to calculate the price return index.



# Index Policy

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## **Index Committee Policy**

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The Index Committee is responsible for setting policy, determining index composition, and administering the indices in accordance with the Indxx index methodology. The Index Committee reserves the right to use qualitative judgment to include, exclude, adjust, or postpone the inclusion of a stock. Continued index membership of a constituent is not necessarily subject to the guidelines provided in each of the Indxx index methodology. A stock may be considered for exclusion by the Index Committee on the basis of corporate governance, accounting policies, lack of transparency and lack of representation, despite meeting all the criteria provided in each of the Indxx index methodology.

## **Announcements**

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Announcements of additions and deletions of constituents, due to various corporate actions mentioned above, in the middle of the year will be decided by the Index Committee. This will be communicated to the client well ahead of time. Also important news items as well as corporate actions with respect to all the constituents of the index will be informed to the client on a weekly basis.

## **Holiday Schedule**

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The index is calculated when the U.S. equity markets are open. In situations where an exchange is forced to close early due to unforeseen events, the index will be calculated based on the closing prices published by the exchange, or if no closing price is available, the last regular trade reported for each stock before the exchange closed.

## Disclaimer

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