

Sustainable management paying off in Hong Kong

The HK Stars Index created by M&E and BDO is showing strong performance, outperforming the broader Hong Kong market. In this latest update, William Cox of M&E, which created the methodology for the index, discusses the leading constituents.

The M&E BDO *Asiamoney* Hong Kong Sustainable Stars Index (HK Stars Index) may be Hong Kong's best performing sustainability-oriented index, outperforming the Hang Seng Index (HSI) by between eight and 18 percentage points since September 2011.

The Stars index is based upon 21 Hong Kong listed stocks from 13 different industries, with 18 of the companies being Hong Kong-based and three headquartered in China. The index measures the sustainable management processes, transparency and financial strength in each company included in the index. Its purpose is to combine a selection of well-managed and financially successful companies, which are as a result more likely to see their stock valuations outperform.

The index's method rewards good equity performance by giving the best managed companies a higher weighting in the index, which was first published by *Asiamoney* in November 2012. This effect means that companies with good management practices, often referred to as sustainable management, will drive the index more strongly than weaker components.

Second rated CLP Power saw an increase in its share price of nearly 15% in 2014. Third rated HKEx's market cap grew by 42% in the same period, while even 21st ranked MTR Holdings improved by 16%. China Mobile, which contributed most to the December 2014 index number, rose by 24% in market cap since the end of January.

The index management scores do not necessarily link to best equity performance, but they do normally link to better equity performance than sectoral peers. Thus, the index as a whole has easily outperformed indices that are based largely on market cap.

Twice a year, M&E, the research and consultancy company that created the index methodology, and BDO, an accountancy firm, decide on whether other companies have improved their processes sufficiently to merit inclusion into the index, normally at the expense of an existing company.

The current Management Value scores of the 21 HK Stars index components are listed in the table opposite. The higher the score, the greater the likelihood of the company producing relatively strong financials and therefore a positive equity price development.

MANAGEMENT VALUE SCORES FOR THE 21 HK STARS INDEX CONSTITUENTS

Rank	Company	M&E Management Value factor
1	Standard Chartered	0.649
2	CLP Power	0.638
3	HKEx	0.600
4	Power Assets	0.598
5	HSBC	0.592
6	Swire	0.591
7	Henderson Land	0.575
8	Prudential	0.565
9	The Link	0.552
10	Hong Kong and Shanghai Hotel	0.547
	Average	0.536
11	Wharf Holdings	0.529
12	Hutchison Whampoa	0.514
13	China Mobile	0.512
14	Manulife	0.501
15	Cheung Kong Holdings	0.499
16	Lenovo	0.498
17	Shangri-La	0.498
18	AIA	0.484
19	Cathay Pacific	0.452
20	Melco Crown	0.445
21	MTR Holdings	0.411

SOURCE: M&E; BDO

TOP FIVES BY CATEGORY

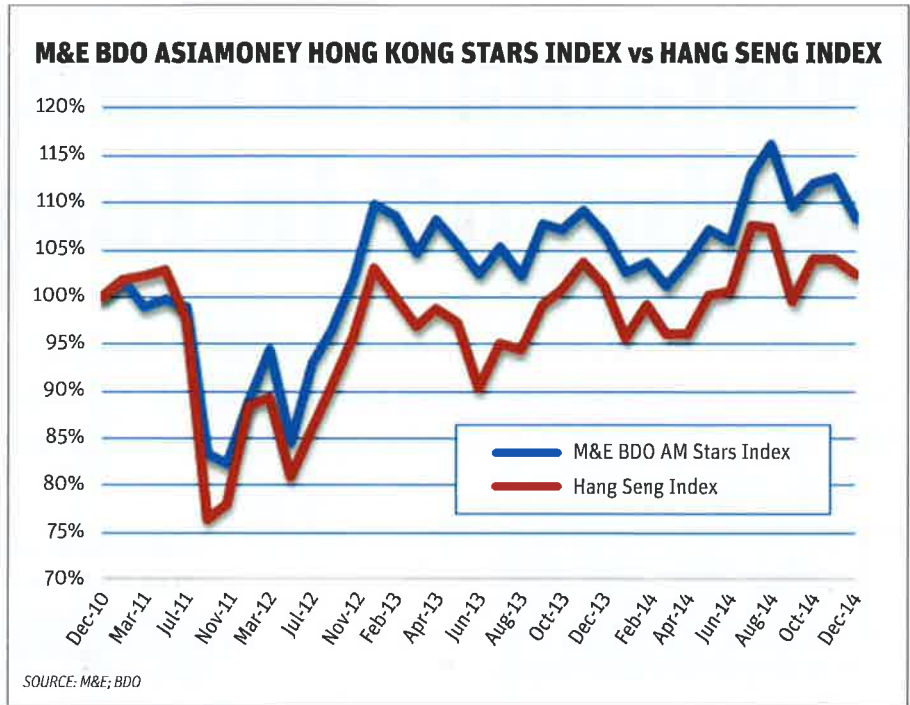
Compliance with good management and governance practices

HK Stars Index components are assessed based on more than 200 compliance points, which cover such areas as governance, transparency and internal processes. Good compliance can help to put processes in place that will help stabilise financial performance.

The only company in the top five of the most compliant to show high volatility in financial performance (see Highest Risk, below) is Lenovo. Good compliance is typical of companies that are components in international sustainability indices, such as HSBC, Standard Chartered and MTR Holdings.

Risk

The risk level reflects volatility in financial performance and certain sustainability indicators of the past three years. Companies with stable revenue streams, such as Power Assets, CLP



Power and Henderson Land. Gradual but consistent growth can also yield a low risk score. High risk scores tend to reflect

high revenue shifts and changes in debt levels such as in the cases of Hong Kong and China companies. ■

GOOD MANAGEMENT AND GOVERNANCE

Rank	Company	Compliance score
1	HSBC	0.780
2	HKEx	0.775
3	Standard Chartered	0.766
4	MTR Holdings	0.766
5	Lenovo	0.766

SOURCE: M&E; BDO

LOWEST RISK

Rank	Company	Risk score
1	Power Assets	0.194
2	China Mobile	0.218
3	Henderson Land	0.225
4	CLP Power	0.226
5	Swire	0.238

SOURCE: M&E; BDO

HIGHEST RISK

Rank	Company	Risk score
1	Lenovo	0.785
2	Manulife	0.771
3	Cathay Pacific	0.556
4	The Link	0.509
5	Wharf Holdings	0.450

SOURCE: M&E; BDO