

The MSCI logo consists of the letters "MSCI" in a white, serif font, set against a dark blue rectangular background.A decorative graphic consisting of two thin, dark blue lines that curve upwards from the left and downwards from the right, meeting at a central point. The lines are positioned above the "Index Methodology" text.

Index Methodology

MSCI Global ESG Indices Methodology

May 2011

1. Introduction

The MSCI Global ESG indices are free float-adjusted market capitalization weighted indices designed to provide exposure to companies that have high Environmental, Social and Governance (ESG) performance. The MSCI Global ESG Indices aim to target sector weights that reflect the relative sector weights of the underlying indices to limit the systematic risk introduced by the ESG selection process.

Currently MSCI constructs MSCI Global ESG Indices for:

- Standard size-segment in all Developed Markets; and
- Small Cap size-segment in the USA.

2. ESG Research Framework

MSCI's ESG research framework generates an analysis and rating of each company's management of its environmental, social and governance performance. The rating criteria address a company's ESG performance in the context of five categories, covering key corporate stakeholders.

- **Environment** – rate a company's management of its environmental challenges, including its effort to reduce or offset the impacts of its products and operations.
- **Community and Society** – measure how well a company manages its impact on the communities where it operates, including its treatment of local population, its handling of human rights issues and its commitment to philanthropic activities.
- **Employees and Supply Chain** – assess a company's record of managing employees, contractors and suppliers. Issues of particular interest include labor-management relations, anti-discrimination policies and practices, employee safety, and the labor rights of workers throughout the company's supply chain.
- **Customers** – measure the quality and safety record of a company's products, its marketing practices, and any involvement in regulatory or anti-competitive controversies.
- **Governance and Ethics** – address a company's investor relations and management practices, including company sustainability reporting, board accountability and business ethics policies and practices.

MSCI applies its proprietary ESG rating framework to each company by selecting the ESG rating criteria most relevant to each firm. To evaluate a company, analysts review more than 500 data points and score more than 100 indicators. MSCI expresses a company's ESG performance as a numerical score and on a letter-based rating scale. The ratings fall on a nine-point scale from AAA to C. Scores and ratings are not normalized across individual industries or the overall company universe. This means that one industry may have no companies that receive any "A" ratings, while another industry may have no companies with "C" ratings.

For more details on ESG scores and ratings, please refer to

http://www.msci.com/products/indices/thematic/esg/esg_research_methodology.html

3. Constructing the MSCI Global ESG Indices

3.1 Underlying Universe

The selection universe for the MSCI Global ESG Indices is defined by the constituents of the MSCI Global Investable Market Indices (GIMI).

3.2 Eligibility Criteria

All constituents of the MSCI Global Investable Market Indices having a company level rating of “B” or above are eligible for inclusion in the MSCI Global ESG Indices.

Companies for which a rating is not available are not eligible for inclusion in the MSCI Global ESG Indices.

3.3 Index Construction

Currently MSCI constructs MSCI Global ESG Indices for:

- Standard size-segment in all Developed Markets; and
- Small Cap size-segment in the USA.

The MSCI Global ESG indices for the Standard size segment are constructed at a regional level, with the exception of North America which is built separately from Canada and the USA. Each regional ESG index targets 50% of the free float adjusted market capitalization of each Global Industry Classification Standard (GICS®) sector of the underlying MSCI Parent Index. These regional ESG indices are then aggregated together to construct the MSCI World ESG Index.

MSCI Regional ESG Index	Region	MSCI Parent Index
MSCI Pacific ESG Index	Developed Asia Pacific	MSCI Pacific
MSCI Europe & Middle East ESG Index	Developed Europe & Middle East	MSCI Europe + Middle East
MSCI Canada ESG Index	Canada	MSCI Canada
MSCI USA ESG Index	USA	MSCI USA

The Large Cap and Mid Cap size segments of the MSCI Global ESG Indices are derived from the Standard size-segment.

The MSCI USA ESG Small Cap index is constructed by targeting 50% of the free float adjusted market capitalization of each sector of the MSCI USA Small Cap Index. The MSCI USA IMI ESG Index is created by aggregating the MSCI USA ESG Index and the MSCI USA ESG Small Cap Index.

4. Maintaining the MSCI Global ESG Indices

4.1 Annual Index Review

The MSCI Global ESG Indices are maintained with the objective of providing exposure to companies that have high ESG performance while seeking to achieve index stability. The composition of the MSCI Global ESG Indices is reviewed on an annual basis in May to coincide with the May Semi-Annual Index Review of the MSCI Global Investable Market Indices. The changes are implemented at the end of May. Ratings used for the annual index review are taken as of the end of April.

At the annual index review, the composition of the MSCI Global ESG Indices is reassessed in order to target 50% free float-adjusted cumulative market capitalization of each sector of the underlying MSCI Parent Index. For each sector, the constituents of the underlying MSCI Parent Index are first ranked based on the company level ESG Score and then by decreasing free float adjusted market capitalization.¹ Constituents for the ESG index are then selected in the following order till the 50% coverage² by cumulative free float adjusted market capitalization target is reached

- Companies in the top 35%
- 'A' rated companies in the top 50%
- Current index constituents in the top 65%
- Remaining Companies in the eligible universe

The above rules are applied sequentially so the ESG index includes companies with high ESG performance, while minimizing turnover.

Any existing index constituent whose rating falls to "CCC" or lower is deleted from the MSCI Global ESG Indices.

4.2 Quarterly Index Reviews

The MSCI Global ESG Indices are also reviewed on a quarterly basis to coincide with the regular Index Reviews (Semi-Annual Index Review in November and Quarterly Index Reviews in February and August) of the MSCI Global Investable Market Indices. The changes are implemented at the end of February, August and November. Ratings used for the quarterly index reviews will be taken as of the end of the month preceding the Index Review, i.e., October, January and July.

At the quarterly index reviews, any existing index constituent whose rating falls to "CCC" or lower is deleted from the MSCI Global ESG Indices. Additions to the indices are only considered in those sectors where the resulting free float adjusted market capitalization coverage does not meet the 50% target. Market price movements may cause small deviations in the sector coverage between two index reviews and so a buffer of 10% [or 5 percentage points] is used to define under-representation, in order to minimize turnover. Companies are added only in those sectors where the current market capitalization coverage is less than 45%, till the 50% target is reached. A company must have a rating of "B" or higher to be considered for addition to the indices.

¹ As a reminder, each company's ESG performance is expressed as a numerical score and a corresponding letter rating.

² The detailed guidelines for achieving the target sector representation of 50% are listed in Appendix 1.

4.3 Ongoing Event-Related Maintenance

The MSCI Corporate Events Methodology is applied for the maintenance of the MSCI Global ESG Indices between Index Reviews. New additions to the underlying index due to corporate events will not be added simultaneously to the MSCI Global ESG Indices, but may be considered for inclusion at the following Index Review. However, companies deleted from the underlying index between Index Reviews are also deleted at the same time from the MSCI Global ESG Indices.

The technical details relating to the handling of specific corporate event types can be found in the MSCI Corporate Events Methodology book available at:

<http://www.msci.com/products/indices/size/standard/methodology.html>

5. Appendix 1: Guidelines on achieving the target sector coverage of 50%

The MSCI Global ESG indices target 50% of the free float adjusted market capitalization of each Global Industry Classification Standard (GICS®) sector of the underlying MSCI Parent Index. The underlying principle in the construction of the index is to achieve sector coverage closest to 50%, while aiming to ensure index stability.

The following guidelines are used in achieving the target sector coverage of 50%:

- For each sector, the constituents of the underlying MSCI Parent Index are first ranked based on the company level ESG score and then by decreasing free float adjusted market capitalization.
- In case of two companies with the same ESG score, an existing index constituent is given preference to maintain index stability. For two existing index constituents with the same ESG score, the larger company by free-float adjusted market capitalization is given preference.
- The cumulative sector coverage at each rank is calculated.
- All companies classified in a sector for which the cumulative coverage is less than 50% will be considered for inclusion in the ESG index in order of decreasing ESG scores.
- MSCI defines the company that increases the cumulative sector coverage above 50% as the 'marginal company'.
- The marginal company will be included in the ESG index only if the absolute difference between the resulting coverage of including the marginal company and the 50% target is lower than the absolute difference between the resulting coverage of not including the marginal company and the 50% target.
- If the marginal company is a current ESG index constituent, then it is retained in the ESG index even though it may result in a cumulative sector coverage significantly higher compared to the 50% target. This is aimed at ensuring better index stability and lower turnover.
- The minimum cumulative sector coverage is set to 45%.
- The marginal company will be added to the ESG index if its non-inclusion would result in cumulative sector coverage of less than 45%.

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The company's flagship product offerings are: the MSCI indices which include over 148,000 daily indices covering more than 70 countries; Barra portfolio risk and performance analytics covering global equity and fixed income markets; RiskMetrics market and credit risk analytics; ISS governance research and outsourced proxy voting and reporting services; FEA valuation models and risk management software for the energy and commodities markets; and CFRA forensic accounting risk research, legal/regulatory risk assessment, and due-diligence. MSCI is headquartered in New York, with research and commercial offices around the world.