

# **MSCI EU PAB Overlay SRI ESG Custom Indexes**

May 2024

## Contents

<b>1. Introduction .....</b>	<b>3</b>
<b>2. Constructing the Indexes .....</b>	<b>4</b>
2.1 Eligible Universe .....	4
2.2 Reference Indexes.....	4
2.3 Eligibility Criteria.....	5
2.2.1 ESG Ratings Eligibility .....	5
2.2.2 ESG Controversies Score Eligibility.....	5
2.2.3 Controversial Business Involvement Criteria .....	5
2.3 Security Selection and Weighting .....	8
2.4 Optimization Constraints.....	8
2.5 Determining the Optimized Index .....	10
2.6 Treatment of Unrated Companies .....	10
<b>3 Maintaining the Indexes.....</b>	<b>11</b>
3.1 Semi Annual Index Reviews .....	11
3.2 Ongoing Event Related Changes .....	11
<b>4 MSCI ESG Research.....</b>	<b>13</b>
4.1 MSCI ESG Ratings .....	13
4.2 MSCI ESG Controversies .....	13
4.3 MSCI Climate Change Metrics .....	13
<b>Appendix I: Calculation of Target Metrics .....</b>	<b>14</b>
<b>Appendix II: Decarbonization Trajectory of Indexes .....</b>	<b>17</b>
<b>Appendix III: Barra Equity Model Used in The Optimization .....</b>	<b>18</b>
<b>Appendix IV: New release of Barra® Equity Model or Barra® Optimizer .....</b>	<b>19</b>
<b>Appendix V: Controversial Business Involvement Criteria .....</b>	<b>20</b>
<b>Appendix VI: Methodology Set.....</b>	<b>23</b>

# 1. Introduction

The MSCI EU PAB Overlay SRI ESG Custom Indexes<sup>1</sup> (the 'Indexes') are designed to represent the performance of companies that are consistent with specific values and climate change based criteria and meet the minimum requirements of the EU Paris-Aligned (PAB)<sup>2</sup> Benchmark.

The Indexes are derived from their corresponding market cap weighted Indexes with applied exclusions based on a variable list provided by JP Morgan Asset Management (the 'Parent Indexes'). This is followed by further exclusions for companies based on their involvement in controversial business activities and an optimization-based approach to apply the PAB requirements.

Exclusions are based on three categories:

- Companies flagged on a variable list provided by JP Morgan Asset Management.
- Companies flagged on their involvement in ESG controversies and their assigned ESG Ratings by MSCI ESG Research.
- Companies flagged for involvement in Controversial Business Activities.

The optimization-based approach aims to:

- Reduce the weighted average greenhouse gas intensity by 50% relative to the Reference<sup>3</sup> Index.
- Reduce the weighted average greenhouse gas (GHG) intensity by 7% on an annualized basis.
- Achieve an ESG Score that is at least aligned with the Reference Index.
- Achieve low turnover and minimize tracking error compared to the Parent Index.

<sup>1</sup> The Indexes are governed by a set of methodology and policy documents ("Methodology Set"), including the present index methodology document. Please refer to Appendix VI for more details

<sup>2</sup> In case there are changes in the EU delegated acts ([Regulation \(EU\) 2016/1011 as amended by Regulation \(EU\) 2019/2089](#)) and an update to the Index methodology is required, MSCI will issue an announcement prior to implementing the changes in the methodology. MSCI will not conduct a formal consultation for such an update.

<sup>3</sup> The Reference Index is the free float-adjusted market capitalization weighted Index which corresponds to the Parent Index. The optimization constraints in Table 3 of Section 2.4 are applied relative to the Reference Index.

## 2. Constructing the Indexes

The Indexes use company ratings and research provided by MSCI ESG Research<sup>4</sup> for the Index construction.

The below table shows the Indexes and their respective Parent and Reference Indexes:

*Table 1: The list of Indexes with their respective Parent and Reference Indexes*

Index Name	Parent Index	Reference Index
MSCI WORLD EU PAB Overlay SRI ESG Custom Index	MSCI World ex Select Securities Index	MSCI World Index
MSCI USA EU PAB Overlay SRI ESG Custom Index	MSCI USA ex Select Securities Index	MSCI USA Index
MSCI Europe EU PAB Overlay SRI ESG Custom Index	MSCI Europe ex Select Securities Index	MSCI Europe Index
MSCI Emerging Markets EU PAB Overlay SRI ESG Custom Index	MSCI Emerging Markets ex Select Securities Index	MSCI Emerging Markets Index

### 2.1 Eligible Universe

The Eligible Universe for the Indexes is constructed from the constituents of the Parent Indexes by excluding securities based on an exclusion list provided by JP Morgan Asset Management. This variable list is updated on a semi-annual basis.

There is one security that will be excluded consistently through the full history of the Indexes.

*Table 2: The security that will be consistently excluded from the Indexes:*

MSCI Security Code	MSCI Security
10600.01	JP Morgan Chase & Co

### 2.2 Reference Indexes

The Reference Indexes aim to represent the Investment Universe for the Parent Index. This Index is the free float-adjusted market capitalization weighted index ("Reference Index") corresponding to the

<sup>4</sup> Please refer to Section 4 for further information regarding the ESG and climate data used in the Index / Indexes that MSCI Limited sources from MSCI ESG Research LLC, a separate subsidiary of MSCI Inc. MSCI ESG Research is solely responsible for the creation, determination, and management of such data. MSCI Limited and MSCI Deutschland GmbH are the benchmark administrators for the MSCI indexes.

Parent Index as per the MSCI Global Investible Markets Index (GIMI) methodology<sup>5</sup>. The constraints in Table 4 of Section 2.4 are applied relative to the Reference Index for this methodology.

## 2.3 Eligibility Criteria

The Indexes use company ratings and research provided by MSCI ESG Research<sup>3</sup> to determine eligibility for index inclusion.

### 2.2.1 ESG Ratings Eligibility

The Indexes use MSCI ESG Ratings to identify companies that have demonstrated an ability to manage their ESG risks and opportunities. Companies are required to have an MSCI ESG Rating Screen of “BB” or above to be eligible for inclusion in the Indexes.

### 2.2.2 ESG Controversies Score Eligibility

The Indexes use MSCI ESG Controversies Scores to identify companies that are involved in very serious controversies associated with the environmental, social, or governance impact of their operations and/or products and services. Companies are required to have an MSCI ESG Controversies Score of 1 or above to be eligible for inclusion in the Indexes.

### 2.2.3 Controversial Business Involvement Criteria

The Indexes use MSCI ESG Business Involvement Screening Research and MSCI Climate Change Metrics to identify companies that are involved in the following business activities. Companies that meet the business involvement criteria are excluded from the Indexes.

- **Controversial Weapons:** Companies involved in Controversial Weapons as defined by the methodology of the MSCI Ex-Controversial Weapons Indexes.
- **ESG Controversies:** All companies assessed as having involvement in ESG controversies that are classified as Red Flags (MSCI ESG Controversy Score of 0). A Red Flag indicates an ongoing, Very Severe ESG controversy implicating a company directly through its actions, products, or operations.
- **Environmental Harm:** All companies assessed as having involvement in environmental controversies that are classified as Red (MSCI Environmental Controversy Score of 0) or Orange Flags (score of 1).
  - A Red Flag indicates an ongoing, Very Severe ESG controversy implicating a company directly through its actions, products, or operations.
  - An Orange Flag indicates an ongoing Severe ESG controversy implicating a company directly, or a Very Severe ESG controversy that is either partially resolved or indirectly attributed to the company’s actions, products, or operations.

<sup>5</sup> For further details regarding the MSCI Global Investible Markets Index methodology, please refer to <https://www.msci.com/index-methodology>

<sup>3</sup> See section 4 for further information regarding ESG and climate data used in the Indexes that MSCI Limited sources from MSCI ESG Research LLC, a separate subsidiary of MSCI Inc. MSCI ESG Research is solely responsible for the creation, determination and management of such data. MSCI Limited and MSCI Deutschland GmbH are the benchmark administrator for the MSCI indexes

- **Thermal Coal Mining**: All companies deriving 1% or more revenue (either reported or estimated) from the mining of thermal coal (including lignite, bituminous, anthracite and steam coal) and its sale to external parties. It excludes revenue from metallurgical coal, coal mined for internal power generation (e.g. in the case of vertically integrated power producers), intra-company sales of mined thermal coal, and revenue from coal trading (either reported or estimated)
- **Oil & Gas**: All companies deriving 10% or more revenue from oil and gas related activities, including distribution / retail, equipment and services, extraction and production, petrochemicals, pipelines and transportation and refining but excluding biofuel production and sales and trading activities.
- **Power Generation**: All companies deriving 50% or more revenue from thermal coal based power generation, liquid fuel based power generation and natural gas based power generation<sup>4</sup>.
- **Tobacco**:
  - All companies that are involved in the production of tobacco products. Tobacco products include nicotine-containing products, including traditional and alternative smoking products.
  - All companies that derive 5% or more reported revenue (or, where not disclosed, maximum estimated revenue) from the production, distribution or retail of tobacco products, as a licensor of brand names for tobacco products, or as a supplier for tobacco products as a percentage of total revenue in its most recently completed fiscal year
- **Adult Entertainment**
  - All companies deriving 5% or more reported revenue (or, where not disclosed, maximum estimated revenue) from the production, distribution or retail of adult entertainment products or services as a percentage of total revenue in its most recently completed fiscal year.
- **Alcohol**
  - All companies deriving 5% or more reported revenue (or, where not disclosed, maximum estimated revenue) from alcohol production as a percentage of total revenue in its most recently completed fiscal year.
  - All companies deriving 15% or more aggregate reported revenue (or, where not disclosed, maximum estimated revenue) from alcohol and related activities as a percentage of total revenue in its most recently completed fiscal year.
- **Gambling**

<sup>4</sup> As per [https://www.ipcc.ch/site/assets/uploads/2018/02/ipcc\\_wg3\\_ar5\\_chapter7.pdf](https://www.ipcc.ch/site/assets/uploads/2018/02/ipcc_wg3_ar5_chapter7.pdf), thermal coal based power generation, liquid fuel based power generation and natural gas based power generation have median lifecycle emissions exceeding 100gCO<sub>2</sub>/kWh.

- All companies deriving 10% or more reported revenue (or, where not disclosed, maximum estimated revenue) from gambling operations, including online or mobile gambling, and supporting activities in its most recently completed fiscal year.
- **Genetically Modified Organisms (GMO)**
  - All companies deriving 5% or more reported revenue (or, where not disclosed, maximum estimated revenue) from activities like genetic engineering as a percentage of total revenue in its most recently completed fiscal year.
- **Nuclear Weapons** All companies involved meeting specific Nuclear Weapons business involvement criteria as described in Appendix V
- **Civilian Firearms**
  - All companies classified as “Producer” of firearms and small arms ammunitions for civilian markets. It does not include companies that cater to the military, government, and law enforcement markets.
  - All companies deriving 5% or more aggregate revenue from the production and distribution (wholesale or retail) of firearms or small arms ammunition intended for civilian use.
- **Conventional Weapons**
  - All companies deriving 5% or revenue (or, where not disclosed, maximum estimated revenue) from conventional weapons, or components, support systems, and services for such products as a percentage of total revenue in its most recently completed fiscal year.
- **Aggregate Weapons**
  - All companies deriving 15% or more aggregate revenue from conventional, controversial and nuclear weapons based on the following categories:
    - Companies involved in the production of conventional weapons, components for such products or support systems and services for such products.
    - Companies involved in the production of biological or chemical weapons, components for such products.
    - Companies involved in the production of blinding laser, incendiary or non-detectable fragments weapons in its most recently completed fiscal year.
    - Companies involved production of nuclear weapons, exclusive and dual-use delivery platform capable to deliver such products, intended and dual-use components of such products, services provided for such products.
- **Nuclear Power**
  - All companies generating 5% or more of their total electricity from nuclear power as a percentage of the company’s total power generation in the most recently completed fiscal year.
  - All companies that have 5% or more of its installed capacity attributed to nuclear power in the most recently completed fiscal year.

- All companies deriving 15% or more reported revenue (or, where not disclosed, maximum estimated revenue) from nuclear power and related activities as a percentage of total revenue in its most recently completed fiscal year.
- **Thermal Coal Power**
  - All companies deriving 5% or more revenue (either reported or estimated) from thermal coal-based power generation.
- **Fossil Fuel Reserves Ownership**
  - All companies with evidence of owning proven & probable coal reserves and/or proven oil and natural gas reserves used for energy purposes, as defined by the methodology of the MSCI Global Ex Fossil Fuels Indexes available at <https://www.msci.com/index-methodology>
- **Fossil Fuel Extraction**

All companies deriving any revenue (either reported or estimated) from thermal coal mining or unconventional oil and gas extraction.

- *Thermal Coal Mining:* Revenue from the mining of thermal coal (including lignite, bituminous, anthracite and steam coal) and its sale to external parties. It does not cover revenue from metallurgical coal; coal mined for internal power generation (e.g. in the case of vertically integrated power producers); intra-company sales of mined thermal coal; and revenue from coal trading.
- *Unconventional Oil & Gas Extraction:* Revenue from oil sands, oil shale (kerogen-rich deposits), shale gas, shale oil, coal seam gas, and coal bed methane. It does not cover all types of conventional oil and gas production including Arctic onshore/offshore, deep water, shallow water and other onshore/offshore.

## 2.3 Security Selection and Weighting

Securities in the Eligible Universe are selected and weighted following an optimization-based approach described below in Section 2.4.

## 2.4 Optimization Constraints

At each Semi-Annual Index Review, the Indexes are constructed using an optimization process that aims to achieve replicability and investability as well as minimize ex-ante tracking error relative to the Parent Index subject to the following constraints:

1. Climate objectives – constraints detailed in Table 3
2. Diversification objectives – constraints detailed in Table 4



Table 3: Constraints imposed to meet ESG & climate objectives:

No.	Climate Objectives	Values
1.	Minimum reduction in Greenhouse Gas (GHG) Intensity relative to EVIC (Scope 1+2+3 <sup>5</sup> ) relative to the Reference Index	50%
2.	Minimum average reduction (per annum) in GHG Intensity (relative to EVIC) relative to GHG Intensity of the index at the Base Date <sup>6</sup>	7%
3.	Minimum active weight in High Climate Impact Sector as defined in Appendix I relative to the Reference Index	0%
4.	Minimum ESG Score Improvement relative to the Reference Index for: <ul style="list-style-type: none"> <li>MSCI World EU PAB Overlay SRI ESG Custom Index</li> <li>MSCI USA EU PAB Overlay SRI ESG Custom Index</li> </ul>	20%
5.	Minimum ESG Score Improvement relative to the Reference Index for: <ul style="list-style-type: none"> <li>MSCI Europe EU PAB Overlay SRI ESG Custom Index</li> <li>MSCI Emerging Markets EU PAB Overlay SRI ESG Custom Index</li> </ul>	At least equivalent

Table 4: Constraints imposed to meet diversification objectives:

No.	Diversification Objective	
6.	Constituent Active Weight relative to the Parent Index	+/- 2%
7.	Security Weight as a multiple of its weight in the Parent Index	20x
8.	Active Sector Weights (the Energy GICS Sector is not constrained) relative to the Parent Index	+/-5%
9.	Active Country Weights relative to the Parent Index <sup>7</sup>	+/-5%
10.	One Way Turnover	5%
11.	Common Factor Risk Aversion	0.0075

<sup>5</sup> Prior to the May 2020 Index Review, the Weighted Average Carbon Emissions Intensity relative to EVIC has been calculated based on Scope 1+2 Emissions.

<sup>6</sup> Prior to the May 2020 Index Review, the average reduction in Weighted Average Carbon Emissions Intensity relative to EVIC has been calculated using Scope 1+2 Emissions since Inception.

<sup>7</sup> In case there are countries in the parent index which weigh less than 2.5% in the parent index then for such countries the active country upper bound of +5% is not applicable. When a country weighs less than 2.5% in parent index then the upper bound of country weight in the Index is set at three times of the country's weight in Parent Index.

No.	Diversification Objective	
12.	Specific Risk Aversion	0.075

During the Semi-Annual Index Review, in the event that there is no optimal solution that satisfies all the optimization constraints, the following constraints will be relaxed, until an optimal solution is found:

- Relax the one-way index turnover constraint in steps of 1% up to 20%.
- Relax the active sector weight constraint in steps of 1% up/down to +/-20%.
- The one-way index turnover constraint and the active sector weight constraint are alternately relaxed until a feasible solution is achieved.

In the event that no optimal solution is found after the above constraint relaxations are exhausted, the relevant Index will not be rebalanced for that Semi-Annual Index Review.

## 2.5 Determining the Optimized Index

The Index is constructed using the Barra Open Optimizer<sup>8</sup> in combination with the relevant Barra Equity Model. The optimization uses the universe of eligible securities and the specified optimization objectives and constraints to determine the constituents of and the weights of constituents in the Indexes.

## 2.6 Treatment of Unrated Companies

Companies not assessed by MSCI ESG Research on data for the following MSCI ESG Research products are not eligible for inclusion in the Indexes:

- MSCI ESG Ratings
- MSCI ESG Controversies

For the treatment of unrated companies in the calculation of target metrics for the optimization, please refer to Appendix I.

<sup>8</sup> Please refer to Appendix III and IV for more details.

## 3 Maintaining the Indexes

### 3.1 Semi Annual Index Reviews

The Indexes are rebalanced on a semi-annual basis, as of the close of the last business day of May and November, coinciding with the May and November Index Review of the Global Investable Market Indexes. The pro forma Indexes are in general announced nine business days before the effective date.

In general, MSCI uses MSCI ESG Research data<sup>9</sup> as of the end of the month preceding the Index Reviews for the rebalancing of the MSCI EU PAB Overlay SRI ESG Custom Indexes. For some securities, such data may not be published by MSCI ESG Research by the end of the month preceding the Index Review. For such securities, MSCI will use ESG data published after the end of month, when available, for the rebalancing of the Indexes.

### 3.2 Ongoing Event Related Changes

The general treatment of corporate events in the Indexes aims to minimize turnover outside of Index Reviews. The methodology aims to appropriately represent an investor's participation in an event based on relevant deal terms and pre-event weighting of the index constituents that are involved. Further, changes in index market capitalization that occur as a result of corporate event implementation will be offset by a corresponding change in the Variable Weighting Factor (VWF) of the constituent.

Additionally, if the frequency of Index Reviews in the Parent Index is greater than the frequency of Index Reviews in the Index, the changes made to the Parent Index during intermediate Index Reviews will be neutralized in the Index.

The following section briefly describes the treatment of common corporate events within the Index.

No new securities will be added (except where noted below) to the Index between Index Reviews. Parent Index deletions will be reflected simultaneously.

#### EVENT TYPE

#### EVENT DETAILS

#### New additions to the Parent Index

A new security added to the Parent Index (such as IPO and other early inclusions) will not be added to the Index.

#### Spin-Offs

All securities created as a result of the spin-off of an existing Index constituent will be added to the Index at the time of event implementation. Reevaluation for continued inclusion in the Index will occur at the subsequent Index Review.

#### Merger/Acquisition

For Mergers and Acquisitions, the acquirer's post event weight will account for the proportionate

<sup>9</sup> See section 4 for details of data sourced from MSCI ESG Research used in the Indexes.

amount of shares involved in deal consideration, while cash proceeds will be invested across the Index.

If an existing Index constituent is acquired by a non-Index constituent, the existing constituent will be deleted from the Index and the acquiring non-constituent will not be added to the Index.

### Changes in Security Characteristics

A security will continue to be an Index constituent if there are changes in characteristics (country, sector, size segment, etc.) Reevaluation for continued inclusion in the Index will occur at the subsequent Index Review.

Further detail and illustration regarding specific treatment of corporate events relevant to this Index can be found in the MSCI Corporate Events Methodology book under the sections detailing the treatment of events in Capped Weighted and Non-Market Capitalization Weighted indexes.

The MSCI Corporate Events methodology book is available at: <https://www.msci.com/index-methodology>.

## 4 MSCI ESG Research

The Indexes are products of MSCI Inc. that utilize information such as company ratings and research produced and provided by MSCI ESG Research LLC (MSCI ESG Research), a subsidiary of MSCI Inc. In particular, the Indexes use the following MSCI ESG Research products: MSCI ESG Ratings, MSCI ESG Controversies, MSCI ESG Business Involvement Screening Research and MSCI Climate Change Metrics. MSCI Indexes are administered by MSCI Limited and MSCI Deutschland GmbH.

### 4.1 MSCI ESG Ratings

MSCI ESG Ratings aim to measure entities' management of environmental, social and governance risks and opportunities. MSCI ESG Ratings use a weighted average key issue calculation that is normalized by industry to arrive at an industry-adjusted ESG score (0-10), which is then translated to a seven-point scale from 'AAA' to 'CCC', indicating how an entity manages relevant key issues relative to industry peers.

The MSCI ESG Ratings methodology can be found at: <https://www.msci.com/legal/disclosures/esg-disclosures>.

### 4.2 MSCI ESG Controversies

MSCI ESG Controversies provide assessments of controversies concerning the potential negative environmental, social, and/or governance impact of company operations, products and services. The evaluation framework used in MSCI ESG Controversies is designed to be consistent with international norms represented by the UN Declaration of Human Rights, the ILO Declaration on Fundamental Principles and Rights at Work, and the UN Global Compact. MSCI ESG Controversies Score falls on a 0-10 scale, with "0" being the most severe controversy.

The MSCI ESG Controversies methodology can be found at: <https://www.msci.com/legal/disclosures/esg-disclosures>

### 4.3 MSCI Climate Change Metrics

MSCI Climate Change Metrics provides climate data & tools to support institutional investors seeking to integrate climate risk & opportunities into their investment strategy and processes. This includes investors seeking to achieve a range of objectives, including measuring and reporting on climate risk exposure, implementing low carbon and fossil fuel-free strategies, alignment with temperature pathways and factoring climate change research into their risk management processes, in particular through climate scenario analysis for both transition and physical risks.

The dataset spans across the four dimensions of a climate strategy: transition risks, green opportunities, physical risks and 1.5° alignment.

For more details on MSCI Climate Change Metrics, please refer to <https://www.msci.com/climate-change-solutions>.

## Appendix I: Calculation of Target Metrics

### Greenhouse Gas (GHG) Emissions Intensity

MSCI ESG Research collects company-specific direct (Scope 1) and indirect (Scope 2) greenhouse gas emissions (GHG) data from company public documents and/or the Carbon Disclosure Project. If a company does not report GHG emissions, then MSCI ESG Research estimates Scope 1 and Scope 2 GHG emissions.

MSCI ESG Research estimates company-specific indirect (Scope 3) GHG emissions from the Scope 3 Carbon Emissions Estimation Model. The data is generally updated on an annual basis.

### Calculation of GHG Intensity

Carbon emissions of a company are normalized for size by dividing annual carbon emissions by Enterprise Value including Cash (EVIC). The Carbon Emissions Intensity is calculated using the latest Scope 1+2 carbon emissions, Scope 3 carbon emissions and EVIC of a company.

Security Level GHG Intensity (Scope 1+2+3) =

$$(\text{Unadjusted Security Level GHG Intensity (Scope 1+2)} + \text{Unadjusted Security Level GHG Intensity (Scope 3)}) * (1 + \text{EVIAF})$$

Unadjusted Security Level GHG Intensity (Scope 1+2) =

$$\frac{(\text{Scope 1} + 2 \text{ Carbon Emissions})}{\text{EVIC (in M\$)}}$$

If Scope 1+2 carbon emissions and/or EVIC are not available, the average Scope 1+2 intensity of all the constituents of the MSCI ACWI in the same GICS Industry Group in which the security belongs is used.

Unadjusted Security Level GHG Intensity (Scope 3) =

$$\frac{(\text{Scope 3 Carbon Emissions})}{\text{EVIC (in M\$)}}$$

If Scope 3 carbon emissions and/or EVIC are not available, the average Scope 3 intensity of all the constituents of the MSCI ACWI in the same GICS Industry Group in which the security belongs is used.

Enterprise Value Inflation Adjustment Factor (EVIAF) =

$$\left( \frac{\text{Average(EVIC)}}{\text{Previous (Average(EVIC))}} \right) - 1$$

Weighted Average GHG Intensity of Parent Index =

$$\sum (Weight\ in\ Parent\ Index * Security\ Level\ GHG\ Intensity)$$

Weighted Average GHG Intensity of Derived Index =

$$\sum (Index\ Weight * Security\ Level\ GHG\ Intensity)$$

### Calculation of Average Decarbonization

On average, the Indexes follow a 7% decarbonization trajectory since the Base Date. The Weighted Average GHG Intensity relative to EVIC at the Base Date ( $W_1$ ) is used to compute the target Weighted Average GHG Intensity relative to EVIC at any given Semi-Annual Index Review ( $W_t$ ) as per the below formula.

$$W_t = W_1 * 0.93^{\frac{(t-1)}{2}}$$

Where 't' is the number of Semi-Annual Index Reviews since the Base Date.

Thus, for the 3<sup>rd</sup> Semi-Annual Index Review since the Base Date (t=3), the target Weighted Average GHG Intensity relative to EVIC will be  $W_1 * 0.93$ .

### Climate Impact Sectors

NACE<sup>10</sup> is the European Union's classification of economic activities. As per the draft DA, stocks in the NACE Section codes A, B, C, D, E, F, G, H, L are classified as "High Climate Impact" sector and other stocks are classified 'Low Climate Impact' sector. The GICS<sup>11</sup> Sub-Industry code for each security is mapped to the corresponding "Climate Impact Sector" using a mapping. This mapping is constructed in the following steps:

1. MSCI has published a mapping<sup>12</sup> between the NACE classes and GICS Sub-Industry.
2. For each GICS Sub-Industry, the number of NACE classes which fall under the High Climate Impact Sector (say the number of classes is  $N_H$ ) and Low Climate Impact Sector (say the number of classes is  $N_L$ ) is identified.
3. If all the NACE classes for a given GICS Sub-Industry are identified in the High Climate Impact Sector ( $N_L = 0$ ), then the GICS Sub-Industry is mapped to the High Climate Impact Sector. Conversely, if all the NACE classes for a given GICS Sub-Industry are identified in the Low Climate Impact Sector ( $N_H = 0$ ) then the GICS Sub-Industry is mapped to the Low Climate Impact Sector.

<sup>10</sup> For further details regarding NACE, please refer to [https://ec.europa.eu/eurostat/statistics-explained/index.php?title=NACE\\_background](https://ec.europa.eu/eurostat/statistics-explained/index.php?title=NACE_background)

<sup>11</sup> GICS, the global industry classification standard jointly developed by MSCI Inc. and S&P Global Market Intelligence.

<sup>12</sup> This mapping is available in the [Handbook of Climate Transition Benchmarks, Paris-Aligned Benchmark and Benchmarks' ESG Disclosures](#). Please note that the mapping does not reflect changes in the GICS structure that were implemented in the MSCI indexes on June 1, 2023.

4. In case a GICS Sub-Industry is mapped to some NACE classes in the High Climate Impact Sector and the others in the Low Climate Impact Sector, the GICS Industry is mapped to the Climate Impact Sector in the following manner:
  - a.  **$N_H \geq N_L$** : If the number of NACE classes in the High Climate Impact Sector is at least equivalent to the number of NACE classes in the Low Climate Impact Sector, the GICS Sub-Industry is mapped to the High Climate Impact Sector.
  - b.  **$N_H < N_L$** : If the number of NACE classes in the High Climate Impact Sector is less than the number of NACE classes in the Low Climate Impact Sector, the GICS Sub-Industry is mapped to the Low Climate Impact Sector.
5. Using the GICS Sub-Industry to Climate Impact Sector mapping created in Step 4, and the security-level GICS Sub-Industry, each security in the Parent Index is classified in either High Climate Impact Sector or Low Climate Impact Sector.



## Appendix II: Decarbonization Trajectory of Indexes

The Weighted Average GHG Intensity on the Base Date ( $W_1$ ) is used to compute the target Weighted Average GHG Intensity at any given Semi-Annual Index Review ( $W_t$ ) as per the below formula.

$$W_t = W_1 * 0.93^{\frac{(t-1)}{2}}$$

Where 't' is the number of Semi-Annual Index Reviews since the Base Date. The table below shows the Weighted Average GHG Intensity on the Base Date ( $W_1$ ) for each of the regions where the Indexes are constructed:

Index	Reference Index	Base Date	$W_1$ (tCO <sub>2</sub> /M\$ Enterprise Value + Cash)
MSCI World EU PAB Overlay SRI ESG Custom Index	MSCI World Index	June 01, 2020	237.79
MSCI USA EU PAB Overlay SRI ESG Custom Index	MSCI USA Index	June 01, 2020	219.99
MSCI Europe EU PAB Overlay SRI ESG Custom Index	MSCI Europe Index	June 01, 2020	270.23
MSCI Emerging Markets EU PAB Overlay SRI ESG Custom Index	MSCI Emerging Markets Index	June 01, 2020	393.21

## Appendix III: Barra Equity Model Used in The Optimization

The MSCI EU PAB Overlay SRI ESG Custom Indexes currently use an optimization setup using the MSCI Barra Global Equity Model for Long-Term Investors (GEMTLTL).

## Appendix IV: New release of Barra® Equity Model or Barra® Optimizer

A major new release of the relevant Barra Equity Model or Barra Optimizer may replace the former version within a suitable timeframe.

## Appendix V: Controversial Business Involvement Criteria

Companies whose activities meet the following values and climate change-based criteria, as evaluated by MSCI ESG Research, are excluded from the MSCI EU PAB Overlay SRI ESG Custom Indexes.

- **Controversial Weapons**

- All companies with any tie to Controversial Weapons (cluster munitions, landmines, depleted uranium weapons, biological/chemical weapons, blinding lasers, non-detectable fragments and incendiary weapons), as defined by the methodology of the MSCI Global Ex-Controversial Weapons Indexes available at <https://www.msci.com/index/methodology/latest/XCW>

- **Civilian Firearms**

- All companies classified as “Producer” of firearms and small arms ammunitions for civilian markets. It does not include companies that cater to the military, government, and law enforcement markets
- All companies deriving 5% or more aggregate revenue from the production and distribution (wholesale or retail) of firearms or small arms ammunition intended for civilian use.

- **Nuclear Weapons**

- All companies that manufacture nuclear warheads and/or whole nuclear missiles.
- All companies that manufacture components that were developed or are significantly modified for exclusive use in nuclear weapons (warheads and missiles).
- All companies that manufacture or assemble delivery platforms that were developed or significantly modified for the exclusive delivery of nuclear weapons.
- All companies that provide auxiliary services related to nuclear weapons.
- All companies that manufacture components that were not developed or not significantly modified for exclusive use in nuclear weapons (warheads and missiles) but can be used in nuclear weapons.
- All companies that manufacture or assemble delivery platforms that were not developed or not significantly modified for the exclusive delivery of nuclear weapons but have the capability to deliver nuclear weapons.
- All companies that manufacture components for nuclear-exclusive delivery platforms.

- **Tobacco**

- All companies classified as a “Producer”.
- All companies deriving 5% or more aggregate revenue from the production, distribution, retail, supply and licensing of tobacco-related products.

- **Adult Entertainment**
  - All companies deriving 5% or more revenue from the production, distribution and retail of adult entertainment materials.
- **Alcohol**
  - All companies deriving 5% or more revenue from the production of alcohol-related products.
  - All companies deriving 15% or more aggregate revenue from the production, distribution, retail and supply of alcohol-related products.
- **Aggregate and Conventional Weapons**
  - All companies deriving 5% or more revenue from the production of conventional weapons and components.
  - All companies deriving 15% or more aggregate revenue from conventional, controversial and nuclear weapons based on the following categories:
    - Companies involved in the production of conventional weapons, components for such products or support systems and services for such products.
    - Companies involved in the production of biological or chemical weapons, components for such products.
    - Companies involved in the production of blinding laser, incendiary or non-detectable fragments weapons in its most recently completed fiscal year.
    - Companies involved production of nuclear weapons, exclusive and dual-use delivery platform capable to deliver such products, intended and dual-use components of such products, services provided for such products.
- **Gambling**
  - All companies deriving 10% or more aggregate revenue from gambling related business activities.
- **Genetically Modified Organisms (GMO)**
  - All companies deriving 5% or more revenue from activities like genetically modifying plants, such as seeds and crops, and other organisms intended for agricultural use or human consumption.
- **Nuclear Power**
  - All companies generating 5% or more of their total electricity from nuclear power in a given year.
  - All companies that have 5% or more of installed capacity attributed to nuclear sources in a given fiscal year.
  - All companies deriving 15% or more aggregate revenue from nuclear power activities.

- **Environmental Harm:** All companies assessed as having involvement in environmental controversies that are classified as Red (MSCI Environmental Controversy Score of 0) or Orange Flags (score of 1).
  - A Red Flag indicates an ongoing, Very Severe ESG controversy implicating a company directly through its actions, products, or operations.
  - An Orange Flag indicates an ongoing Severe ESG controversy implicating a company directly, or a Very Severe ESG controversy that is either partially resolved or indirectly attributed to the company's actions, products, or operations.

- **Fossil Fuel Reserves Ownership**

- All companies with evidence of owning proven & probable coal reserves and/or proven oil and natural gas reserves used for energy purposes, as defined by the methodology of the MSCI Global Ex Fossil Fuels Indexes available at <https://www.msci.com/index-methodology>

- **Fossil Fuel Extraction**

All companies deriving any revenue (either reported or estimated) from thermal coal mining or unconventional oil and gas extraction.

*Thermal Coal Mining:* Revenue from the mining of thermal coal (including lignite, bituminous, anthracite and steam coal) and its sale to external parties. It does not cover revenue from metallurgical coal; coal mined for internal power generation (e.g. in the case of vertically integrated power producers); intra-company sales of mined thermal coal; and revenue from coal trading.

*Unconventional Oil & Gas Extraction:* Revenue from oil sands, oil shale (kerogen-rich deposits), shale gas, shale oil, coal seam gas, and coal bed methane. It does not cover all types of conventional oil and gas production including Arctic onshore/offshore, deep water, shallow water and other onshore/offshore.

- **Thermal Coal Power**

- All companies deriving 5% or more revenue (either reported or estimated) from thermal coal-based power generation.

- **Oil & Gas**

- All companies deriving 10% or more revenue from oil and gas related activities, including distribution / retail, equipment and services, extraction and production, pipelines and transportation and refining but excluding biofuel production and sales and trading activities

- **Power Generation**

All companies deriving 50% or more revenue from thermal coal based power generation, liquid fuel based power generation and natural gas based power generation<sup>13</sup>

<sup>13</sup> As per [https://www.ipcc.ch/site/assets/uploads/2018/02/ipcc\\_wg3\\_ar5\\_chapter7.pdf](https://www.ipcc.ch/site/assets/uploads/2018/02/ipcc_wg3_ar5_chapter7.pdf), thermal coal based power generation, liquid fuel based power generation and natural gas based power generation have median lifecycle emissions exceeding 100gCO<sub>2</sub>/kWh.

## Appendix VI: Methodology Set

The Indexes are governed by a set of methodology and policy documents (“Methodology Set”), including the present index methodology document as mentioned below:

- Description of methodology set – <https://www.msci.com/index/methodology/latest/ReadMe>
- MSCI Corporate Events Methodology – <https://www.msci.com/index/methodology/latest/CE>
- MSCI Fundamental Data Methodology – <https://www.msci.com/index/methodology/latest/FundData>
- MSCI Index Calculation Methodology – <https://www.msci.com/index/methodology/latest/IndexCalc>
- MSCI Index Glossary of Terms – <https://www.msci.com/index/methodology/latest/IndexGlossary>
- MSCI Index Policies – <https://www.msci.com/index/methodology/latest/IndexPolicy>
- MSCI Global Industry Classification Standard (GICS) Methodology – <https://www.msci.com/index/methodology/latest/GICS>
- MSCI Global Investable Market Indexes Methodology – <https://www.msci.com/index/methodology/latest/GIMI>
- MSCI Global ex Controversial Weapons Indexes Methodology – <https://www.msci.com/index/methodology/latest/XCW>
- MSCI SRI Indexes Methodology – <https://www.msci.com/index/methodology/latest/SRI>
- MSCI EU CTB/PAB Overlay Indexes Methodology – <https://www.msci.com/index/methodology/latest/MSCIEUCTBPABOverlay>
- ESG Factors In Methodology\*

The Methodology Set for the Indexes can also be accessed from MSCI’s webpage <https://www.msci.com/index-methodology> in the section ‘Search Methodology by Index Name or Index Code’.

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