

# FAQ on the Transition Announcement for the MSCI High Dividend Yield Indices

Announcement sent on January 29, 2013

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## Summary of the announcement

The MSCI High Dividend Yield Indices will transition to the enhanced methodology as part of the May 2013 Semi-Annual Index Review.

The enhancements to the existing MSCI High Dividend Yield Index methodology incorporate additional screens that exclude stocks based on certain "quality" characteristics and recent 12 month price performance. The quality scores are calculated using fundamental variables such as Return on Equity, Earnings Variability and Debt to Equity. These enhancements aim to exclude stocks with potentially deteriorating fundamentals that may force them to cut or reduce dividends. The MSCI High Dividend Yield Indices will continue to be based on free float adjusted market capitalization weights.

In addition, the dividend persistence screen will be applied to MSCI High Dividend Yield Indices based on Emerging Markets starting from the May 2013 Semi-Annual Index Review as well. The dividend persistence screen excludes securities with shrinking dividends and is currently applied only on MSCI High Dividend Yield Indices based on Developed Markets.

An updated methodology book, including a description of the enhanced methodology to be applied from the May 2013 Semi-Annual Review in Appendix III, is available on the MSCI web site, [http://www.msci.com/products/indices/strategy/risk\\_premia/hdy/](http://www.msci.com/products/indices/strategy/risk_premia/hdy/).

This FAQ complements the announcement and provides more details around the rationale for the enhanced methodology, the transition process itself and the official transition date.

## Questions and Answers

### 1. Why is MSCI implementing these enhancements to the existing MSCI High Dividend Yield Index methodology?

Following extensive consultations with the investment community in 2012, MSCI has decided to enhance the MSCI High Dividend Yield Index methodology by incorporating additional screens that exclude stocks based on certain "quality" characteristics and recent 12 month price performance. The quality scores are calculated using fundamental variables such as Return on Equity, Earnings Variability and Debt to Equity. These enhancements aim to exclude stocks with potentially deteriorating fundamentals that may force them to cut or reduce dividends.

### 2. Are there any immediate changes as a result of the announcement?

No. All MSCI High Dividend Yield (HDY) Indices will continue to be calculated and maintained according to the current methodology until the transition to the enhanced methodology is completed at the May 2013 Semi-Annual Index Review (SAIR).

### 3. Which MSCI High Dividend Yield Indices are affected by the announcement?

All existing standard MSCI High Dividend Yield Indices based on the MSCI High Dividend Yield Indices methodology will transition to the enhanced methodology as part of the May 2013 SAIR. They will continue to be calculated and maintained according to the current methodology until the transition to the enhanced methodology is completed at the May 2013 SAIR.

### 4. How will MSCI determine the constituents of the MSCI High Dividend Yield Indices at the May 2013 SAIR?

The following enhanced methodology will be applied at the time of the transition of the existing MSCI High Dividend Yield Indices to the enhanced methodology during the May 2013 SAIR.

Any new constituent will have to satisfy the following criteria to be eligible for inclusion in the pro forma MSCI High Dividend Yield Index:

1. Quality Screen : Quality score > 0
2. Price Performance Screen: 1-year Price Performance not within the bottom 5% of the universe of securities with negative 1-year price performance.
3. Dividend Persistence Screen: 5-year DPS growth > 0
4. Dividend Sustainability Screen: Payout not within top 5% of the universe of stocks with positive payout
5. Dividend Yield Screen : Dividend Yield > 1.3 times Parent Index Dividend Yield

Note that the Quality Screen would not be applied for MSCI High Dividend Yield Indices based on MSCI Parent Indices that include securities from the small cap size segment.

In addition, the Dividend Persistence Screen will be applied to MSCI High Dividend Yield Indices based on Emerging Markets starting from the May 2013 Semi-Annual Index Review as well. The Dividend Persistence Screen excludes securities with shrinking dividends and is currently applied only on MSCI High Dividend Yield Indices based on Developed Markets.

**5. Would buffers be applied to existing constituents of the MSCI High Dividend Yield Indices as part of the transition to the enhanced MSCI High Dividend Yield Index methodology?**

Yes. Any existing constituent would have to satisfy the following criteria to be eligible to be retained in the pro forma MSCI High Dividend Yield Index:

1. Quality Screen : Quality score  $> -0.5$
2. Price Performance Screen: 1-year Price Performance not within the bottom 5% of the universe of securities with negative 1-year price performance.
3. Dividend Persistence Screen: 5-year DPS growth  $\geq 0$ ; if 5-year DPS growth  $< 0$ , then 1-year DPS growth  $\geq 0$
4. Dividend Sustainability Screen: Payout not within top 2% of the universe of stocks with positive payout
5. Dividend Yield Screen : Dividend Yield  $>$  Parent Index Dividend Yield

**6. What is the indicative turnover associated with the transition?**

Based on the simulated transition analysis as of the November 2012 SAIR, for the MSCI World High Dividend Yield Index, the one-way transition turnover was 8.68% as compared to the actual one-way turnover of 5.62% for the existing MSCI World High Dividend Yield Index at the November, 2012 SAIR. For the MSCI ACWI High Dividend Yield Index, the simulated one-way transition turnover was 14.4% as compared to the actual one-way turnover of 4.79% for the existing MSCI ACWI High Dividend Yield Index at the November, 2012 SAIR.

**7. Currently the Dividend Persistence Screen is not applied in Emerging Markets. Will this change?**

Yes. The Dividend Persistence Screen will be applied to MSCI High Dividend Yield Indices based on Emerging Markets starting from the May 2013 Semi-Annual Index Review as well. The Dividend Persistence Screen excludes securities with shrinking dividends and is currently applied only on MSCI High Dividend Yield Indices based on Developed Markets.

**8. Currently the Dividend Persistence Screen is not applied in the small cap segment. Will this change?**

No. The Dividend Persistence Screen will not be applied in the small cap segment with the exception of the USA and Australia.

**9. When and where will MSCI announce the results of the transition?**

The pro forma index constituents will be distributed to subscribing clients through regular product files as of the close of May 21, 2013.

(Enhanced High Dividend Yield indices will be available through MSCI's Enhanced Index modules ,Risk Premia Standard/IMI Modules, or individual subscription(s). Index levels will be posted as for the current MSCI High Dividend Yield Indices on msci.com)

**10. Will MSCI provide any indication of the results of the transition prior to the May 2013 SAIR?**

Yes. Starting April 30, 2013, indicative list of constituents will be made available to clients upon request for the following MSCI High Dividend Yield Indices:

- MSCI World High Dividend Yield Index,
- MSCI EM High Dividend Yield Index,
- MSCI ACWI High Dividend Yield Index,
- MSCI USA High Dividend Yield Index,
- MSCI Europe High Dividend Yield Index,
- MSCI EMU High Dividend Yield Index,
- MSCI AC Asia ex Japan High Dividend Yield Index,
- MSCI Japan High Dividend Yield Index and
- MSCI Kokusai High Dividend Yield Index.

These indicative constituent lists will be provided in excel format on request by clients. Please note that these indicative constituents may or may not be eligible for inclusion in final pro forma MSCI High Dividend Yield Indices at the May 2013 SAIR.

**11. Will MSCI provide provisional indices based on the enhanced methodology prior to the May 2013 SAIR?**

No. The transition will be implemented in one step as part of the May 2013 SAIR and no provisional indices will be provided prior to the transition.

**12. Will there be any change to the branding of the MSCI High Dividend Yield Indices?**

No. The existing MSCI High Dividend Yield indices will transition to the enhanced MSCI High Dividend Yield Index methodology at the May 2013 SAIR and there will be no change to the branding of the existing MSCI High Dividend Yield Indices.

**13. I subscribe to an MSCI High Dividend Yield Index but prefer not to apply the enhancements to the MSCI High Dividend Yield Index methodology. Is it possible?**

Yes. All MSCI High Dividend Yield Indices will transition to the enhanced methodology, however clients who do not wish to apply all or certain of the enhancements to the MSCI High Dividend Yield Indices may subscribe to custom indices.

Custom indices are also available to clients who would like securities to be screened based on different thresholds than those applied in the enhanced MSCI High Dividend Yield Indices methodology.

**14. How can existing clients of custom High Dividend Yield indices migrate to the enhanced High Dividend Yield methodology if preferred?**

Existing clients of custom High Dividend Yield indices have the option to implement the enhancements of the MSCI High Dividend Yield Index methodology in whole or in part or to make no change to the existing custom index methodologies at the May 2013 SAIR. They need to notify the MSCI custom index team in advance in the event of making changes to the existing custom index methodologies for the May 2013 SAIR.

**15. Will MSCI provide a simulated history for the MSCI High Dividend Yield Indices based on the enhanced MSCI High Dividend Yield Index methodology?**

Yes. Starting March 15, 2013, MSCI will provide simulated index level history on request for selected MSCI High Dividend Yield Indices based on the enhanced MSCI High Dividend Yield Index methodology. The simulated history will provide at least 10 years of index level history. The simulated index level history will be available in an Excel file upon request through MSCI client service.

The MSCI High Dividend Yield Indices for which history will be made available are:

- MSCI World High Dividend Yield Index,
- MSCI EM (Emerging Markets) High Dividend Yield Index,
- MSCI ACWI High Dividend Yield Index,
- MSCI USA High Dividend Yield Index,
- MSCI Europe High Dividend Yield Index,
- MSCI EMU High Dividend Yield Index,
- MSCI AC Asia ex Japan High Dividend Yield Index,
- MSCI Japan High Dividend Yield Index and
- MSCI Kokusai High Dividend Yield Index.

**16. Who will be eligible to receive the simulated history mentioned in question 15?**

Existing clients subscribing to MSCI Risk Premia Standard/IMI Modules, or individual MSCI High Dividend Yield Indices are eligible to receive the simulated history mentioned in question 15 for the above mentioned indices on demand.

## Client Service Information is Available 24 Hours a Day

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<sup>1</sup>As of March 31, 2012, as published by eVestment, Lipper and Bloomberg in September 2012