

## **Methodology Book For:**

- **MSCI EUR HY Select Corporate Bond Index**
- **MSCI EUR HY Sustainable SRI Select Corporate Bond Index**

**June 2023**

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# 1 Introduction

The MSCI EUR HY Sustainable SRI Select Corporate Bond Index (the “Index”) is constructed from the MSCI EUR HY Select Corporate Bond Index (the “Parent Index”) by incorporating business exclusion screens based on involvement in Controversial Weapons, Civilian Firearms, Nuclear Weapons, Tobacco, Adult Entertainment, Alcohol, Conventional Weapons, Gambling, Genetically Modified Organisms, Nuclear Power, Fossil Fuel Reserves, Fossil Fuel Extraction, Thermal Coal Based Power Generation, ESG Controversy Score and ESG Rating. The issuers weights are subsequently capped at 3%.

The Parent Index is constructed from the global credit universe of Corporate Bonds denominated in EUR by applying various selection criteria based on security type, credit rating, bond size, maturity and country of domicile.

## 2 Index Construction Methodology

Constructing the Index involves the following steps:

- Defining the MSCI EUR HY Select Corporate Bond Index
- Defining the MSCI EUR HY Sustainable SRI Select Corporate Bond Index

### 2.1 Defining the MSCI EUR HY Select Corporate Bond Index

The Parent Index is constructed using the methodology defined for MSCI EUR HY Corporate Bond Index in the MSCI Corporate Bond Indexes Methodology<sup>1</sup> except for the below changes:

- At rebalancing, each security included in the Parent Index will have a notional amount outstanding greater than or equal to EUR 400 million.
- Issuer Country of Domicile: Securities included in the Parent Index must belong to issuers domiciled in the Developed Market countries defined in Appendix I.
- Regulation S bonds are eligible for inclusion and 144a bonds are ineligible for inclusion in the Parent Index.
- Each Parent Index constituent must be rated either by S&P or Moody's. For bonds that are rated by both S&P and Moody's, the lower rating will be used to determine the index inclusion criteria:

| S&P Rating              |                        | Moody's Rating          |                        |
|-------------------------|------------------------|-------------------------|------------------------|
| Higher Rating Threshold | Lower Rating Threshold | Higher Rating Threshold | Lower Rating Threshold |
| BB+                     | B-                     | Ba1                     | B3                     |

- Callable Perpetual Bonds are eligible for inclusion in the Parent Index.
- Junior Subordinated Bonds belonging to Banks (based on GICS Industry Group classification) are excluded from the index.

<sup>1</sup> Refer to MSCI Corporate Bond Indexes Methodology available at: <https://www.msci.com/index-methodology>

## 2.2 Defining the MSCI EUR HY Sustainable SRI Select Corporate Bond Index

The Index is constructed from the Parent Index by applying the screening criteria defined in Appendix II. The exclusions are based on the data provided by MSCI ESG Research at the time of index rebalancing. The screened securities which are eligible for inclusion in the Index are weighted in proportion of their weight in the Parent Index. The issuers weights are subsequently capped at 3%<sup>2</sup>.

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<sup>2</sup> The issuer capping is relaxed in steps of 1% if capping at 3% is infeasible.

## 3 Index Rebalancing & Maintenance

### 3.1 Monthly Index Reviews of the MSCI EUR HY Select Corporate Bond Index

- The composition of the Parent Index is reviewed monthly, with Rebalancing Date being first business date of the month.
- Change in the index composition is based on latest data available as of three days prior to the Rebalancing Date, which is defined as the Cut-Off Date.
- MSCI will announce proforma index rebalancing results as of the Cut-Off Date.
- Bonds are added to or deleted from the index only on monthly rebalancing dates, except in case of an exchange event<sup>3</sup>. For the existing index components any changes to index eligibility will only be reflected in the next monthly rebalancing.
- Any inclusion or exclusion criteria satisfied for a given security in the universe, after the Cut-Off Date, will generally become effective at the following monthly rebalancing; should conditions remain unchanged.
- Any cash that accrues within the index in each month is re-invested on a pro-rata basis across the index constituents, on the Rebalancing Date. In essence, cash in the index is swept out on rebalancing and the opening index portfolio on the Rebalancing Date starts with zero accrued cash balance.
- Certain variants of total return calculation of the index on the Rebalancing Date may be adjusted for transaction cost<sup>4</sup> as securities are added to the index at the offer price.

For further information on index total return calculation and corporate events handling please refer to the MSCI Fixed Income Index Calculation Methodology. For the holiday calendar used in the indexes, please refer to the MSCI Fixed Income Data Methodology.<sup>5</sup>

<sup>3</sup> Refer to the MSCI Fixed Income Index Calculation Methodology for detail

<sup>4</sup> Refer to the MSCI Fixed Income Index Calculation Methodology for detail

<sup>5</sup> The methodologies are available at: <https://www.msci.com/index-methodology>

MSCI leverages the GICS<sup>®6</sup> sector classification framework for construction of the Parent Index. Please refer to MSCI GICS Methodology<sup>7</sup> for details.

### 3.2 Monthly Index Reviews of the MSCI EUR HY Sustainable SRI Select Corporate Bond Index

The Index is reviewed on a monthly basis to coincide with the Monthly Index Review of the Parent Index. In general, the pro forma index is announced three business days before the effective date. In general, MSCI uses latest available MSCI ESG Research data on the announcement date for the rebalancing of the Indexes.

At each Monthly Index Review, the eligible universe is updated, and the composition of the index is reassessed based on the defined methodology.

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<sup>6</sup> GICS, the global industry classification standard, jointly developed by MSCI Inc. and S&P Global.

<sup>7</sup> The GICS methodology is available at: <https://www.msci.com/gics>

## 4 MSCI ESG Research

The Indexes use company ratings and research provided by MSCI ESG Research. 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.

For details on MSCI ESG Research's full suite of ESG products, please refer to: <https://www.msci.com/esg-investing>.

### 4.1 MSCI ESG RATINGS

MSCI ESG Ratings aim to measure entities' management of environmental, social and governance risks and opportunities. MSCI ESG Ratings are based on 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/esg-and-climate-methodologies>.

### 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 in: <https://www.msci.com/esg-and-climate-methodologies>.

### 4.3 MSCI ESG BUSINESS INVOLVEMENT SCREENING RESEARCH

MSCI ESG Business Involvement Screening Research (BISR) aims to enable institutional investors to manage environmental, social and governance (ESG) standards and restrictions reliably and efficiently.

For more details on MSCI ESG Business Involvement Screening Research, please refer to [http://www.msci.com/resources/factsheets/MSCI\\_ESG\\_BISR.pdf](http://www.msci.com/resources/factsheets/MSCI_ESG_BISR.pdf).



## Appendix I: List of Developed Market Countries

| Country Name |
|--------------|
| Australia    |
| Austria      |
| Belgium      |
| Canada       |
| Croatia      |
| Cyprus       |
| Denmark      |
| Estonia      |
| Finland      |
| France       |
| Germany      |
| Greece       |
| Hong Kong    |
| Iceland      |
| Ireland      |
| Israel       |
| Italy        |
| Japan        |
| Latvia       |
| Lithuania    |
| Luxembourg   |
| Macao Sar    |
| Malta        |
| Netherlands  |
| New Zealand  |

|                                 |
|---------------------------------|
| <b>Norway</b>                   |
| <b>Portugal</b>                 |
| <b>Singapore</b>                |
| <b>Slovakia</b>                 |
| <b>Slovenia</b>                 |
| <b>Spain</b>                    |
| <b>Sweden</b>                   |
| <b>Switzerland</b>              |
| <b>United Kingdom</b>           |
| <b>United States of America</b> |

## Appendix II: ESG-based Exclusion Criteria

### Controversial Weapons:

- All companies with any tie to Controversial Weapons as defined below:
  - Cluster Bombs
    - MSCI ESG Research's cluster bomb research identifies public companies that are involved in the production of cluster bombs and munitions, or the essential components of these products.
  - Landmines
    - MSCI ESG Research's landmines research identifies public companies that are involved in the production of anti - personnel landmines, anti - vehicle landmines, or the essential components of these products.
  - Depleted Uranium Weapons
    - MSCI ESG Research's depleted uranium weapons research identifies public companies involved in the production of depleted uranium weapons and armor.
  - Chemical and Biological Weapons
    - MSCI ESG Research's chemical and biological weapons research identifies public companies that are involved in the production of chemical and biological weapons, or the essential components of these products.
  - Blinding Laser Weapons
    - MSCI ESG Research's blinding laser weapons research identifies public companies that are involved in the production of weapons utilizing laser technology to cause permanent blindness.
  - Non-Detectable Fragments
    - MSCI ESG Research's non-detectable fragments research identifies public companies that are involved in the production of weapons that use non-detectable fragments to inflict injury.
  - Incendiary Weapons (White Phosphorus)
    - MSCI ESG Research's incendiary weapons research identifies companies that are involved in the production of weapons using white phosphorus.

**Involvement criteria:**

- Producers of the weapons
- Producers of key components of the weapons (only applies to cluster bombs, landmines, depleted uranium weapons as well as chemical and biological weapons)
- Ownership of 20% or more of a weapons or components producer

The minimum limit is raised to 50% for financial companies having an ownership in a company that manufactures controversial weapons or key components of controversial weapons

- Owned 50% or more by a company involved in weapons or components production

**Revenue limits:**

- Any identifiable revenues, i.e., zero tolerance

**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 of adult entertainment materials
- All companies deriving 15% or more aggregate 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

#### **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 weapons systems, components, and support systems and services

#### **Gambling:**

- All companies deriving 5% or more revenue from ownership of operation of gambling-related business activities

- All companies deriving 15% 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

#### **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 and 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.

**ESG Controversies:**

- All companies having faced very severe controversies pertaining to ESG issues – defined as companies with an ESG Controversy Score of 0.

**ESG Rating:**

- Securities of companies having an MSCI ESG Rating of “BB”, “B”, “CCC” or unrated.

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