

MSCI Growth Target EU PAB Indexes Methodology

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1 Introduction

The MSCI Growth Target EU PAB Indexes (the “Indexes”) are designed to represent the performance of a strategy that meets the minimum standards of the EU Paris Aligned Benchmark (PAB)¹ and seek higher exposure to the Growth style factor relative to other factors from the relevant Barra Equity Model² while maintaining market risk exposure similar to the underlying Parent Index (herein, the “Parent Index”)³.

This Index methodology aims to incorporate climate-based constraints in an optimization-based index construction approach by using risk-target optimization.

¹ On December 3, 2020, the European Commission has published the delegated acts in the Official Journal (<https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32020R1818&from=EN>) which contain the minimum technical requirements for the EU Paris-aligned Benchmarks. In case there are changes in the EU delegated acts 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.

² Please refer to Appendix II

³ The Indexes are governed by a set of methodology and policy documents (“Methodology Set”), including the present index methodology document. The Methodology Set for the Indexes can be accessed from MSCI’s webpage <https://www.msci.com/index-methodology> in the section ‘Search Methodology by Index Name or Index Code’.

The Methodology Set includes a document ‘ESG Factors in Methodology’ that contains the list of environmental, social, and governance factors considered, and how they are applied in the methodology (e.g., selection, weighting or exclusion)

2 Constructing the Indexes

The Indexes are constructed based on an optimization process from the underlying Parent Index using a Barra Equity Model to maximize the Index-level exposure to the targeted style factors while maintaining market risk equal to or lower than that of the Parent Index and meeting the minimum standards required of EU Paris Aligned Benchmarks (PAB).

The Indexes use company ratings and research provided by MSCI ESG Research⁴ for the Index construction.

The steps for constructing the Indexes are described below.

2.1 Applicable Universe

The Applicable Universe includes all the existing constituents of an underlying MSCI Parent Index. The relevant Parent Index could be any MSCI Global Investable Market Index.

2.2 Eligible Universe

The Eligible Universe is constructed by excluding securities from the Applicable Universe based on the exclusion criteria described below.

2.3 Defining the Exclusion Criteria

2.3.1 Controversy Based Exclusion Criteria

Securities of companies assessed as having involvement in ESG controversies that are classified as Red Flags (MSCI ESG Controversy Score of 0) are excluded. A Red Flag indicates an ongoing Very Severe ESG controversy implicating a company directly through its actions, products, or operations.

2.3.2 Business Exclusion Criteria

Companies that are involved in specific businesses which have high potential for negative social and/or environmental impact are ineligible for inclusion in the Index.

- Controversial Weapons
- Environmental Harm
- Tobacco
- Thermal Coal Mining
- Oil & Gas
- Power Generation
- Thermal Coal Distribution

⁴ 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 is the benchmark administrator for the MSCI indexes.

Please refer to Appendix I for more details on these criteria.

2.4 Treatment of Unrated Companies

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

- MSCI ESG Controversies
- MSCI Climate Change Metrics
- MSCI Business Involvement Screening Research (BISR)

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

2.5 Constituent Identification

The selection of constituents from the Eligible Universe is conducted through the process of optimization.

The optimization relies on the factor exposures for all the securities in the Parent Index and the factor covariance matrix of the relevant Barra Equity Model. The optimization is performed using a base currency. The default currency is the US Dollar.

2.6 Weighting Scheme

The optimization objective is to maximize the Alpha score (representative of the exposures to the Growth factor) under constraints on the active exposure to the nontarget factors and the “target risk” constraint where the risk target is equal to the ex-ante risk of the Parent Index at the time of rebalancing.

2.6.1 Calculation of the Alpha Score

$$\alpha_i = F_{G,i}$$

Where,

$F_{G,i}$ = Growth factor exposure of each security i .

The factor exposures for the target factors are sourced as follows:

- Growth – The factor exposure for each security taken from the relevant Barra Equity Model. The factor definition is given in Appendix II.

2.7 Optimization Constraints

At each Index Review of the Index, the following optimization constraints are employed, which aim to ensure investability while achieving total risk in line with that of the Parent Index:

- The maximum weight of an Index constituent will be restricted to the lower of (the weight of the security in the Parent Index +2%) or 10 times the weight of the security in the Parent Index. The minimum weight of an Index constituent will be restricted to the higher of the (weight of the security in the Parent Index -2%) or 0.

- The Global Industry Classification Standard (GICS®)⁵ sector weights of the Index will not deviate more than +/- 5% from the sector weights of the Parent Index (the Energy GICS Sector is not constrained).
- For countries with weight greater than 2.5% in the Parent Index, the weight in the Index will not deviate more than +/-5% from the country weight in the Parent Index.
- For countries with weight less than 2.5% in the Parent Index, the weight in the Index will be capped at 3 times their weight in the Parent Index.
- The above country weight constraint will also apply on China A Stock Connect listings as a group separately in addition to the usual country weight constraint on China.
- The exposure of the Index to non-target Barra style factors relative to the Parent Index will be constrained as below:
- Exposure to Book-to-Price, Earnings Yield, Long-Term Reversal, Dividend Yield, Momentum, Profitability, Earnings Quality, Investment Quality and Mid-Capitalization factors will be constrained to be within the range of 0 to 0.25 standard deviations relative to the Parent Index.
- Exposure to Beta, Residual Volatility, Earnings Variability, Leverage and Size factors will be constrained to be within the range of -0.25 to 0 standard deviations relative to the Parent Index.
- Exposure to Liquidity factor will be constrained to be within the range of - 0.25 to 0.25 standard deviations relative to the Parent Index.
- The one-way turnover of the Index is constrained to a maximum of 20% at each Index Review.
- In addition to the above-mentioned constraints, the climate objective constraints are applied as detailed in Table 1 below:

Table 1: Constraints imposed to meet climate objectives

No.	Climate Objectives	
1.	Minimum reduction in Greenhouse Gas (GHG) Intensity relative to EVIC (Scope 1+2+3 ⁶) relative to the Parent Index	50%

⁵ The Global Industry Classification Standard (GICS) was developed by and is the exclusive property of MSCI and S&P Global Market Intelligence.

⁶ Prior to the May 2020 Index Review of the Indexes, the Weighted Average Carbon Emissions Intensity relative to EVIC has been calculated based on Scope 1+2 Emissions.

2.	Minimum average reduction (per annum) in GHG Intensity (relative to EVIC) relative to GHG Intensity of the Index at the Base Date ⁷	7%
3.	Minimum active weight in High Climate Impact Sector ⁸ relative to Parent Index	0%

2.8 Determining the Optimized Index

The Indexes are constructed using the Barra Open Optimizer in combination with the relevant Barra Equity Model⁹. The optimization uses the Eligible Universe and the Applicable Universe and the specified optimization objective and constraints to determine the constituents and the weights of the Index. The Eligible Universe is used to determine the securities eligible in the Index and the Applicable Universe is used to define other constraints like “target risk”. Infeasible optimizations are handled as explained in Appendix V.

⁷ Prior to the May 2020 Index Review of the Indexes, the average reduction in Weighted Average Carbon Emissions Intensity relative to EVIC has been calculated using Scope 1+2 Emissions since Inception.

⁸ For further details on how MSCI assigns companies to either the high or low climate impact sectors, please refer to the MSCI EU CTB/PAB Index Framework available on <https://www.msci.com/index/methodology/latest/EUCTBPABIndexFramework>.

⁹ Please refer to Appendix IV for the detailed information on model usage

3 Maintaining the Indexes

3.1 Index Reviews

The Indexes are reviewed on a semi-annual basis, usually as of the close of the last business day of May and November, coinciding with the regular Index Reviews of the MSCI Global Investable Market Indexes. The Barra Equity Model data as of the end of April and October are used respectively. This approach aims to capture timely updates to the risk characteristics of the companies and coincide with the rebalancing frequency of the relevant Parent Index.

In general, MSCI uses MSCI ESG Research data¹⁰ (including MSCI ESG Controversies, MSCI ESG Business Involvement Screening Research and MSCI Climate Change Metrics) as of the end of the month preceding the Index Reviews for the rebalancing of the Indexes. The pro forma Indexes are in general announced nine business days before the effective date.

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.

¹⁰ See section 4 for details of data sourced from MSCI ESG Research used in the Indexes.

For Mergers and Acquisitions, the acquirer's post event weight will account for the proportionate 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 MSCI EU CTB Overlay Indexes and the MSCI EU PAB Overlay 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 Climate Change Metrics, MSCI ESG Controversies and MSCI ESG Business Involvement Screening Research. MSCI Indexes are administered by MSCI Limited and MSCI Deutschland GmbH.

4.1 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.

4.1.1 Fossil Fuels and Power Generation Metrics

MSCI ESG Research identifies companies involved in fossil fuel-related assets and activities including fossil fuel reserves, resource extraction, power generation and generation capacity, revenue from such assets and activities and capital investments in such assets and activities. The metrics are based on disclosed activities, disclosed revenue and estimates of revenue that are extrapolated from company disclosures and eligible third-party sources (such as NGOs).

4.1.2 Greenhouse Gas (GHG) Emissions

MSCI ESG Research collects reported emissions and uses proprietary estimation methodologies that follows the GHG Protocol in including carbon dioxide (CO₂) and the five other principal GHGs: hydrofluorocarbons (HFCs), methane (CH₄), nitrous oxide (N₂O), perfluorocarbons (PFCs), and sulfur hexafluoride (SF₆). Emissions of these other gases are accounted for in terms of the quantity of CO₂ that has an equivalent global warming potential.

For more details on MSCI Climate Change Metrics, please refer to:

<https://www.msci.com/legal/disclosures/climate-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 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.

The MSCI Business Involvement Screening Research methodology can be found at:
<https://www.msci.com/legal/disclosures/esg-disclosures>.

Appendix I: Business Exclusion Criteria

Companies whose activities meet the following values and climate change-based criteria, as evaluated by MSCI ESG Research, are excluded from the MSCI Growth Target EU PAB Indexes:

- **ESG Controversy Score (“Red Flags”)**
 - Securities of companies assessed as having involvement in ESG controversies that are classified as Red Flags (MSCI ESG Controversy Score of 0) are excluded. A Red Flag indicates an ongoing Very Severe ESG controversy implicating a company directly through its actions, products, or operations. For more details on MSCI ESG Controversies Score, please refer to: <https://www.msci.com/esg-and-climate-methodologies>.
- **Controversial Weapons Involvement**
 - 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 Ex-Controversial Weapons Indexes available at <https://www.msci.com/index/methodology/latest/XCW>
- **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.
- **Tobacco**
 - All companies that are involved in the manufacturing of Tobacco products.
- **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), intracompany 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, 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 generation¹¹.

- **Thermal Coal Distribution**

- All companies with evidence of thermal coal distribution or transport involvement. This includes transport of thermal coal by road, rail, shipping or air, and physical trading of thermal coal. It does not include involvement in storage of thermal coal, or involvement in metallurgical coal-related activities.

¹¹ As per 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 100gCO2/kWh.

Appendix II: Target Factor Definition Summary

The style factor targeted in the MSCI Growth Target EU PAB Index is the Growth factor which is described using factor score from the current release of the MSCI Barra Equity Model. The model data will be used from previous end-of-month, prior to the rebalancing date. Following is the definition of the Growth factor currently used in the Index. For more detailed information on individual factors in GEMTL, please refer to <https://www.msci.com/portfolio-management>.

Growth:

The Growth factor adopts the definition from the relevant Barra Equity Factor Model (currently GEMTL). Based on the definition from the current GEMTL model, the factor score for each security is based on earnings growth-based and sales growth-based valuation metrics - captured by the following three descriptors: Analyst-Predicted Long-Term Earnings Growth (EGRLF), Earnings Per Share Growth Rate (EGRO) and Sales Per Share Growth Rate (SGRO).

$$\text{Growth}_i = (0.7) * \text{EGRLF}_i + (0.1) * \text{EGRO}_i + (0.2) * \text{SGRO}_i$$

Appendix III: 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) =

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

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 GICS¹² 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) =

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

¹² GICS is the global industry classification standard jointly developed by MSCI and S&P Global Market Intelligence.

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 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 Index Reviews since the Base Date.

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

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

The methodology presently uses MSCI Barra Global Equity Model for Long-Term Investors (“GEMTL”) for the optimization. A new release of the relevant Barra Equity Model or Barra Optimizer may replace the former version within a suitable timeframe.

Appendix V: Handling Infeasible Optimizations

During the Index Review, in the event that there is no optimal solution that satisfies all the optimization constraints defined in Section 2.6, the following constraints will be relaxed, until an optimal solution is found:

- Relax the turnover constraint in steps of 2% up to a maximum of 30%.
- Relax the maximum weight multiple in steps of 2 up to a maximum of 5 iterations based upon the following formula:

$$wm_{i+1} = step + wm_i \text{ for } i = 0 - 4$$

Where wm_i = Maximum Active weight multiple

$$wm_0 = 10$$

- The maximum turnover constraint and the maximum weight multiple constraint are alternately relaxed until a feasible solution is achieved. For example, constraints relaxation is executed in the sequence as illustrated below:

Order of Relaxation	Maximum Asset Weight Multiple	Turnover Limit
1	10 times the weight of the security in the Parent Index	22%
2	12 times the weight of the security in the Parent Index	22%
3	12 times the weight of the security in the Parent Index	24%
4	14 times the weight of the security in the Parent Index	24%

In the event that no optimal solution is found after the above constraints have been relaxed over all the iterations, the relevant MSCI Growth Target PAB Index will not be rebalanced for that Index Review.

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 – <http://www.msci.com/index/methodology/latest/XCW>
- 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’.

* ‘ESG Factors in Methodology’ contains the list of environmental, social, and governance factors considered, and how they are applied in the methodology (e.g., selection, weighting or exclusion). It can be accessed in the Methodology Set as described above.

Appendix VII: Changes to this Document

The following sections have been modified as of July 2023:

- Methodology book was updated to reflect the transition of the MSCI Global Investable Market Indexes (GIMI) to Quarterly Comprehensive Index Reviews.
- All references to “Semi-Annual Index Reviews” and “Quarterly Index Reviews” of the MSCI GIMI were replaced with “Index Reviews.”
- Section 2.3.1, Appendix I:
Clarified the exclusion criteria for companies involved in ESG Controversies
- Section 4: MSCI ESG Research
Moved section after the Section 3
Updated descriptions of MSCI ESG Research products.

The following sections have been modified as of May 2025:

- Section 2.3.2 Business Exclusion Criteria
Added Thermal Coal Distribution
- Section 2.4: Treatment of Unrated Companies
Added the treatment of companies when ESG controversies, business involvement screening research or climate change metrics research is not available from MSCI ESG Research.
- Section 2.7: Optimization Constraints
Added footnote referring to the MSCI EU CTB/PAB Index Framework in relation to Climate Impact Sector
- Appendix I: Values and Climate Change Based Screening Criteria
Added the description for Thermal Coal distribution screen
- Appendix III: Calculation of Target Metrics
Removed definition of Climate Impact Sectors
- Appendix VI: Methodology Set
Added details on the Methodology Set of the Index

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