

CONSULTATION ON THE TREATMENT OF SPECIFIC INDEXES IN THE CONTEXT OF CHINA A PARTIAL INCLUSION

- MSCI EM 50 Index
- MSCI China 50 Index
- MSCI China Free Index
- MSCI All China Index

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INTRODUCTION

- The partial inclusion of China A shares to the MSCI Emerging Markets Indexes at the May 2018 Semi-Annual Index Review may impact a number of MSCI Indexes.
- In this context, MSCI is launching a consultation on the following proposals:
 - Include China A shares as well as B shares to the eligible universe of the MSCI EM 50 Index, MSCI China 50 Index and MSCI China Free Indexes
 - Not to include China A "Stock Connect" listings but retain the onshore China A Shares in the MSCI All China Indexes effective June 1, 2018.
- In addition, MSCI proposes to transition the MSCI All China Indexes to the MSCI China All Shares Indexes effective June 1, 2019.
- MSCI welcomes feedback from the investment community on the proposal on or before February 23, 2018.
- Please note that this consultation may or may not result in any changes to the MSCI Indexes or methodologies. Consultation feedback will remain confidential. MSCI may publicly disclose feedback if specifically requested by respective market participants. In that case, the relevant feedback would be published together with the final results of the consultation.

INCLUDING A SHARES AND B SHARES TO

- MSCI EM 50 INDEX
- MSCI CHINA 50 INDEX
- MSCI CHINA FREE INDEX

SUMMARY OF INDEX CONSTRUCTION AND OBJECTIVES

- China B shares have been historically excluded from the MSCI EM 50 Index, MSCI China 50 Index and MSCI China Free Index.
- MSCI EM 50 Index and MSCI China 50 Index:
 - The MSCI EM 50 Index is a more tradable version of the MSCI Emerging Markets Index and is composed of just 50 of its largest constituents. The index applies eligibility criteria to exclude some of the smallest Emerging Markets countries and uses depositary receipts for certain markets that are less accessible to foreign investors. The index also excludes Real Estate Investment Trusts (REITs) and China B shares.
 - The MSCI China 50 Index includes 50 of the largest constituents of the MSCI China Index, but exclude B shares.
 - The eligible securities in both indexes are ranked in the decreasing order of free float-adjusted market capitalization
- The MSCI China Free Indexes are based on the MSCI China Indexes, but exclude B shares. The indexes are composed of Hong Kong-listed Chinese companies including H shares, Red chips, P chips and foreign listed shares.

PROPOSALS: MSCI EM 50 & MSCI CHINA 50

Proposal for the MSCI EM 50 Index and MSCI China 50 Index:

- In the context of the partial inclusion of China A shares to the MSCI Emerging Markets Indexes, MSCI proposes to include China A shares as well as B shares to the eligible universe of the MSCI EM 50 Index and MSCI China 50 Index, coinciding with the inclusion of China A shares in the MSCI Emerging Markets Index on June 1, 2018.
- The security selection and weighting of A shares would be based on the free float-adjusted market capitalization after the application of the Partial Inclusion.
- SIMULATED IMPACT: As of December 29, 2017, no A shares (based on 5% inclusion factor) and B shares would be added to the MSCI EM 50 Index and MSCI China 50 Index
- **Discussion:**
 - Should MSCI include both China A shares and B shares to the MSCI EM 50 Index and MSCI China 50 Index?
 - Should the security selection of A shares be based on free-float adjusted market cap after application of partial inclusion factor?

PROPOSALS: MSCI CHINA FREE INDEX

Proposal for the MSCI China Free Index:

- MSCI proposes to include China A shares and B shares to the MSCI China Free Index
- The proposal is based on the positive impact on the accessibility of the China A market of both the Stock Connect program and the loosening by the local Chinese stock exchanges of pre-approval requirements that can restrict the creation of index-linked investment vehicles globally.
- **Discussion:** Should MSCI include both China A shares and B shares to the MSCI China Free Index?

TRANSITION OF THE MSCI ALL CHINA INDEXES TO MSCI CHINA ALL SHARES INDEXES

BACKGROUND

- The MSCI All China Indexes aim to achieve a broader representation of the global China investment opportunity set by combining various complementary China Indexes. Currently, the indexes cover all listed China share classes as follows:
 - A shares local listing included in the MSCI China A Indexes*
 - B shares, H shares, Red-chips, P-chips and foreign listed Chinese companies included in MSCI China Indexes
 - Additional foreign listed Chinese companies included in the MSCI Overseas China Indexes but not in the MSCI China Indexes
- The **MSCI China All Shares** Index is constructed based on one integrated China equity universe.
 - While it also aims at representing all listed China share classes it also benefits from a single methodology, fully consistent with the MSCI Global Investable Market Indexes framework

DIFFERENCES WITH MSCI CHINA ALL SHARES INDEXES

- Below illustrates a simulated impact of the potential transition from the MSCI All China Indexes to the MSCI China All Shares Indexes

| | MSCI All China | | | MSCI China All Shares | | | # Securities | | One Way Index Turnover* |
|--|------------------|------------|---------------|-----------------------|------------|---------------|--------------|------------|-------------------------|
| | Index Market Cap | # Sec. | Weight | Index Market Cap | # Sec. | Weight | Add | Del | |
| Total Index | 3,550,483 | 954 | 100.0% | 2,705,607 | 654 | 100.0% | 58 | 358 | 19.3% |
| B shares, H shares, Red-chips, P-chips | 1,162,071 | 137 | 32.7% | 1,222,248 | 192 | 45.2% | 55 | 0 | |
| Foreign listings | 403,373 | 16 | 11.4% | 403,983 | 18 | 14.9% | 3 | 1 | |
| A shares | 1,985,039 | 801 | 55.9% | 1,079,376 | 444 | 39.9% | 0 | 357 | |

Note: All market caps are in USD millions. Data as of the close of December 12, 2017

- The differences in index constituents and weights between the two indexes are due to the following methodological differences:

| | MSCI All China Index | MSCI China All shares Index |
|---------------------|--|---|
| Universe definition | Composite Index, combining several methodologies | Single integrated universe |
| Foreign listings | Based on both MSCI GIMI* and MSCI Overseas China methodologies | Based on the MSCI GIMI Methodology |
| A shares inclusion | Based on the Domestic Inclusion Factor (DIF) | Based on Foreign Inclusion Factor (FIF) |

* MSCI Global Investable Market Indexes

PROPOSAL

- Following the partial inclusion of China A shares in the MSCI Emerging Markets Index, MSCI proposes not to include China A "Stock Connect" listings but retain the onshore China A Shares in the MSCI All China Indexes effective June 1, 2018.
- MSCI proposes to transition the MSCI All China Indexes to the MSCI China All Shares Indexes effective June 1, 2019.
- **Benefits:**
 - Align two index methodologies with similar objectives
 - Choose the methodology fully governed by the GIMI framework
 - Discontinue an index based on the multiple methodologies, which is not consistent with a potential further A shares inclusion in the future
- **Discussion:**
 - Should MSCI consider aligning the MSCI All China Indexes with the MSCI China All Shares Indexes?

OPTIONS FOR TRANSITION

PROPOSAL

Transition the MSCI All China Indexes to MSCI China All Shares Indexes effective June 1, 2019

Option 1

- Keep the name of “MSCI All China Index”
- Move to MSCI China All Shares Index Methodology

Option 2

- Rename the index to “MSCI China All Shares Index”
- Move to MSCI China All Shares Index Methodology

Option 3

- Transition to existing “MSCI China All Shares Index”
- Discontinue the “MSCI All China Index”

- Discussion:

- Should MSCI All China Indexes be renamed to MSCI China All Shares Indexes following the methodology change?
- Can the MSCI All China Indexes be discontinued?

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Our line of products and services includes indexes, analytical models, data, real estate benchmarks and ESG research.

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