

Consultation on Decarbonization Trajectory Adjustments for MSCI Equity CTB/PAB Indexes

ADDRESSING SIGNIFICANT CHANGES IN THE
CALCULATION METHODOLOGY OF GHG INTENSITY

February 2025

This consultation may or may not lead to the implementation of any or all of the proposed changes in the highlighted or any other MSCI indexes. Consultation feedback will remain confidential. MSCI may publicly disclose feedback if specifically requested by specific market participants. In that case, the relevant feedback would be published together with the final results of the consultation.

Summary

- **MSCI proposes a default approach to adjust the targeted decarbonization trajectory of MSCI equity CTB/PAB indexes**
- Such adjustments would be made following **significant changes to the calculation methodology of GHG intensity, which require a change in base date** (Article 8(2) of Commission Delegated Regulation (EU) 2020/1818)
 - Scope covers both index methodology changes and emissions data methodology changes
 - Significance established through quantitative and/or qualitative criteria
- Under the proposed **default treatment, the decarbonization trajectory would be adjusted for the effects of the calculation methodology changes**. This approach aims for:
 - **Continuity**: the trajectory remains anchored to the original decarbonization start date
 - **Credibility**: the index continues to target the same % emissions reduction by 2050
 - **Consistency**: the trajectory reflects the same (latest) calculation methodology of GHG intensity
- MSCI proposes to apply the default treatment to the MSCI EU CTB/PAB Overlay, MSCI Climate Change and MSCI Climate Paris Aligned index methodologies*
- MSCI invites feedback from market participants on or before March 7, 2025 and will announce the results of the consultation by the end of March 2025.

Conditions for Changes in CTB/PAB Base Dates

BACKGROUND CONTEXT – NOT FOR CONSULTATION

Conditions for Changes in Base Dates (1/2)

Commission Delegated Regulation (EU) 2020/1818, Article 8(2):
“Significant changes in the calculation methodology of GHG intensity” require setting a new base date

“Changes in the calculation methodology of GHG intensity” include:

1) Changes in emissions data methodology, e.g.:

- approach to raw data sourcing
- estimation models (Scope 1&2, Scope 3)

2) Changes in index methodology, e.g.:

- calculation of security-level emissions intensity
- index-level aggregation of emissions intensity



Conditions for Changes in Base Dates (2/2)

Commission Delegated Regulation (EU) 2020/1818, Article 8(2):
“**Significant changes in the calculation methodology of GHG intensity**” require setting a new base date

→ New base date whenever *changes in the calculation methodology of GHG intensity* (as defined on the previous slide) are assessed as **quantitatively or qualitatively significant**:

	Quantitative Significance	Qualitative Significance
Condition	Impact of the methodology change on the GHG intensity equivalent to 3 years or more of CTB/PAB annual decarbonization ¹	Conceptual change in calculation and interpretation of index-level GHG intensity
Scope: Changes to the index methodology	Yes	Yes, if material and conceptual change (e.g. changes in calculation logic)
Scope: Changes to the MSCI ESG Research emissions data methodology	Yes	Yes, if material and conceptual change (e.g. changes to definitions of data points)
Granularity	Evaluated for each CTB/PAB index individually , based on the impact on the GHG intensity of the investable universe of the index, at its decarbonization start date	Evaluated jointly for all CTB/PAB indexes affected by the change

Proposal: Adjustments to Targeted Decarbonization Trajectories of CTB/PAB Indexes

Overview of the Proposal

- MSCI proposes to apply a **default approach** to adjust the targeted decarbonization trajectory of **equity CTB/PAB indexes** at the time of the change in base date.

Proposal – Default Approach	What the Proposal Aims to Achieve
Adjust the decarbonization trajectory to where it would have been, had the new methodology been applied since the original decarbonization start date.	<ul style="list-style-type: none">• Continuity: the trajectory remains anchored to the original decarbonization start date• Credibility: the index continues to target the same % emissions reduction by 2050• Consistency: the trajectory reflects the same (latest) calculation methodology of GHG intensity

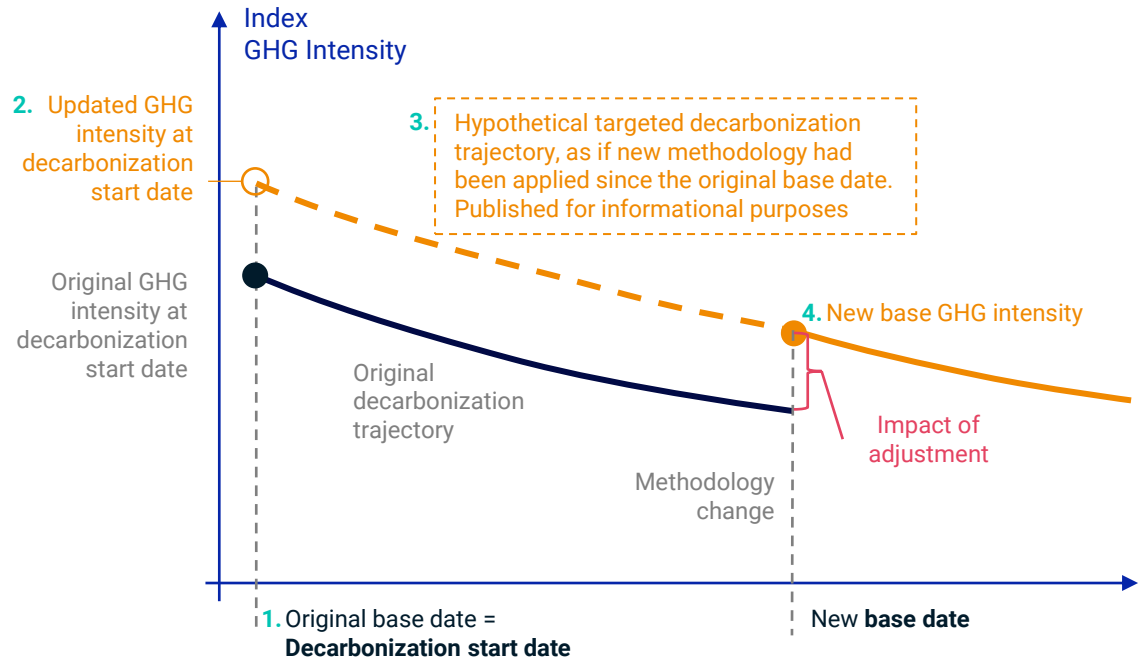
- MSCI proposes to apply the default treatment to the MSCI EU CTB/PAB Overlay, MSCI Climate Change and MSCI Climate Paris Aligned index methodologies*

Illustration of the Proposal

Aim: reflect the decarbonization trajectory as-if the new methodology had been applied since the original base date

Proposed adjustment approach:

- 1. Decarbonization start date** (=original base date) **does not change**
- 2. GHG intensity at the decarbonization start date is recalculated** according to the new methodology*
- 3. Hypothetical targeted decarbonization trajectory** is calculated by applying the annual decarbonization rate since the decarbonization start date (=original base date), with the GHG intensity recalculated with the new methodology
- 4. New base date:** Date when adjustment is applied
New base GHG intensity: Target GHG intensity value at the new base date



Conceptual Scope of Decarbonization Trajectory Adjustments

What is adjusted for?

- Index methodology changes affecting the GHG intensity calculation
- Changes to emissions data due to “model” and “methodology” updates by MSCI ESG Research, e.g.
 - Changes to model granularity, configuration and parameters

What is not adjusted for?

- “Data changes” by MSCI ESG Research, e.g.
 - Changes in company-reported emissions data
 - Changes in other company-reported data used for emissions estimates

Adjustments only meant to mitigate the effect of methodological changes

Adjusted trajectories still fully incorporate changes in actual company emissions since the decarbonization start date

Regulatory Considerations

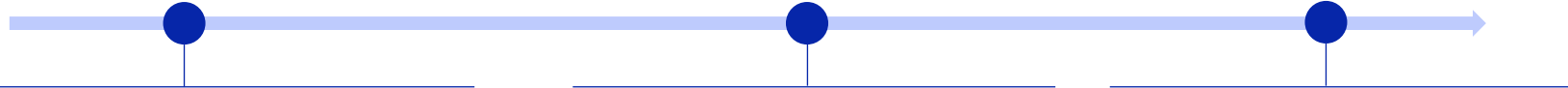
Commission Delegated Regulation (EU) 2020/1818, Article 8(2):
“Significant changes in the calculation methodology of GHG intensity” require setting a new base date

- Adjustment proposal distinguishes:
 - **Index decarbonization start date:** Conceptual starting point of decarbonization trajectory, remains unchanged
 - **“Base date” reported for regulatory purposes** reflects the date of the last adjustment
- **Updated decarbonization trajectory applies going forward;** historical intensities are not restated
- For transparency, MSCI may **publish the simulated historical targeted decarbonization trajectory**, reflecting the new emissions methodology (see Appendix for a possible example)
- Proposed adjustment approach would become part of MSCI EU CTB/PAB Index Framework¹ and would be referenced in the relevant index methodologies

Simulated Impact of the Proposal

Historical “Significant” Changes to the Calculation Methodology of GHG Intensity

- **Qualitatively**, across standard equity CTB/PAB index methodologies*, there have been **no significant changes** to the calculation methodology of the GHG intensity **since June 2020** (no **conceptual** changes to index calculation or emissions data methodologies).
- **Quantitatively**, several **historical changes to the scope 3 estimation methodology** from MSCI ESG Research had **significant impact on certain CTB/PAB indexes**. Relevant changes include e.g.:



February 2021: Update of Scope 3 Category 11 estimates:

- Change to a new sector classification, providing more granularity esp. for manufacturing industries
- Switch from revenue-based to production-based estimates for mining, refining, transportation

April 2022: Update of Scope 3 Category 10 estimates:

- More granular assessment of mining industries
- New emissions factors for processing of raw materials, esp. iron ore and precious metals

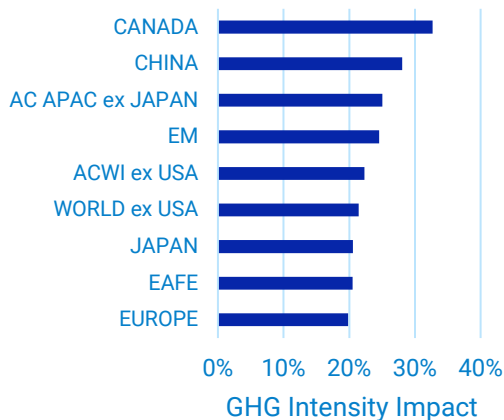
October 2023:

- Alignment of reference years of inputs to scope 3 estimates
- Time-dependent emission factors in commodity sectors
- Revenue-based estimation for integrated oil and gas companies

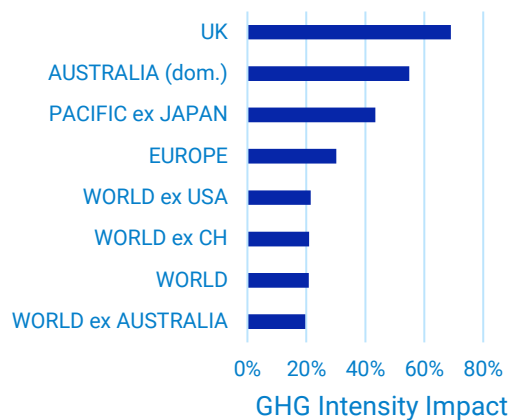
Quantitatively Significant Data Methodology Changes

Simulated list of **parent indexes** (“investable universes”) and **decarbonization start dates** used in **standard** MSCI equity CTB/PAB indexes*, where the **cumulative impact of scope 3 estimation methodology changes** applied by MSCI ESG Research **since the decarbonization start date is considered quantitatively significant**

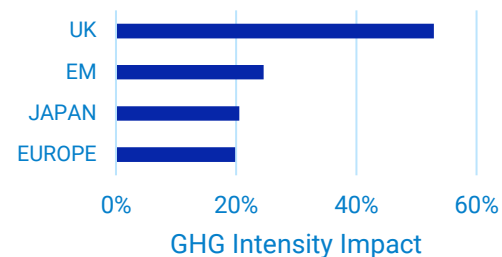
Climate Paris Aligned** (decarb start 06/2020)



Climate Change (decarb start 06/2021)



EU CTB/PAB Overlay (decarb start 06/2020)



3y decarbonization ≈ 20% impact
5y decarbonization ≈ 30% impact
7y decarbonization ≈ 40% impact

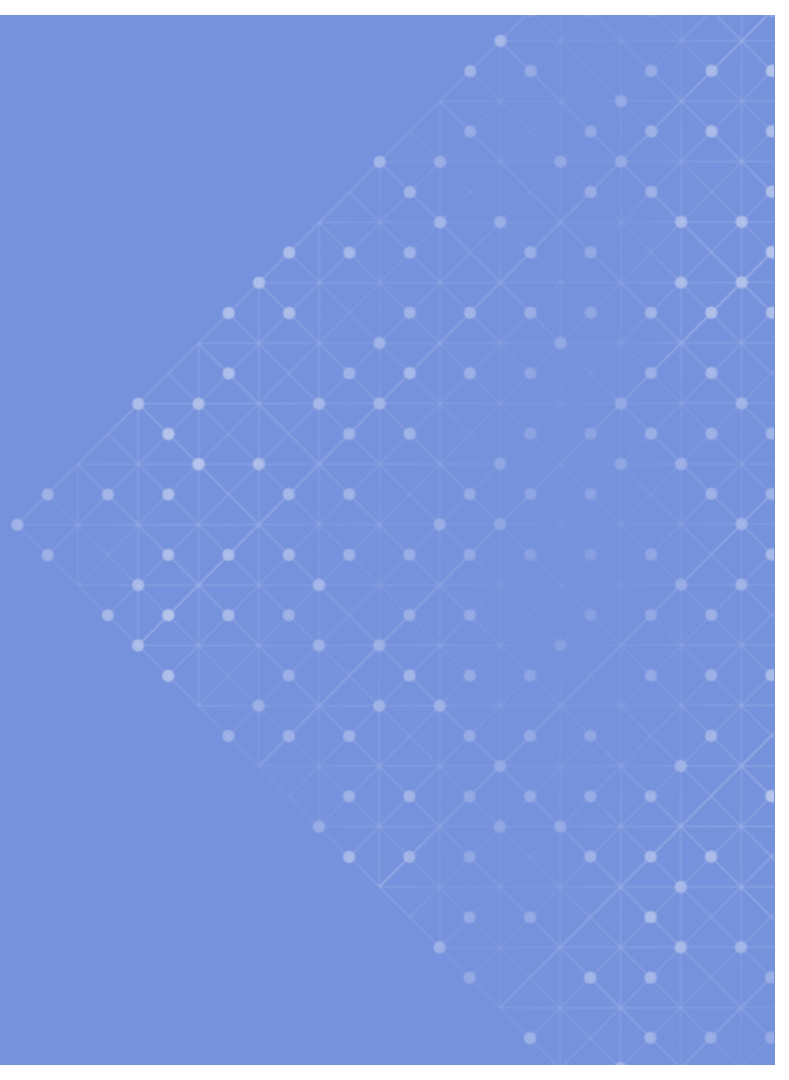
Based on simulation, these indexes would be in scope for a decarbonization trajectory adjustment under the Proposal



* MSCI equity CTB/PAB indexes included in the MSCI ESG Standard and MSCI ESG IMI Modules

** Note that the Climate Paris Aligned indexes follow a 10% year-on-year decarbonization trajectory which exceeds the 7% year-on-year regulatory requirement.

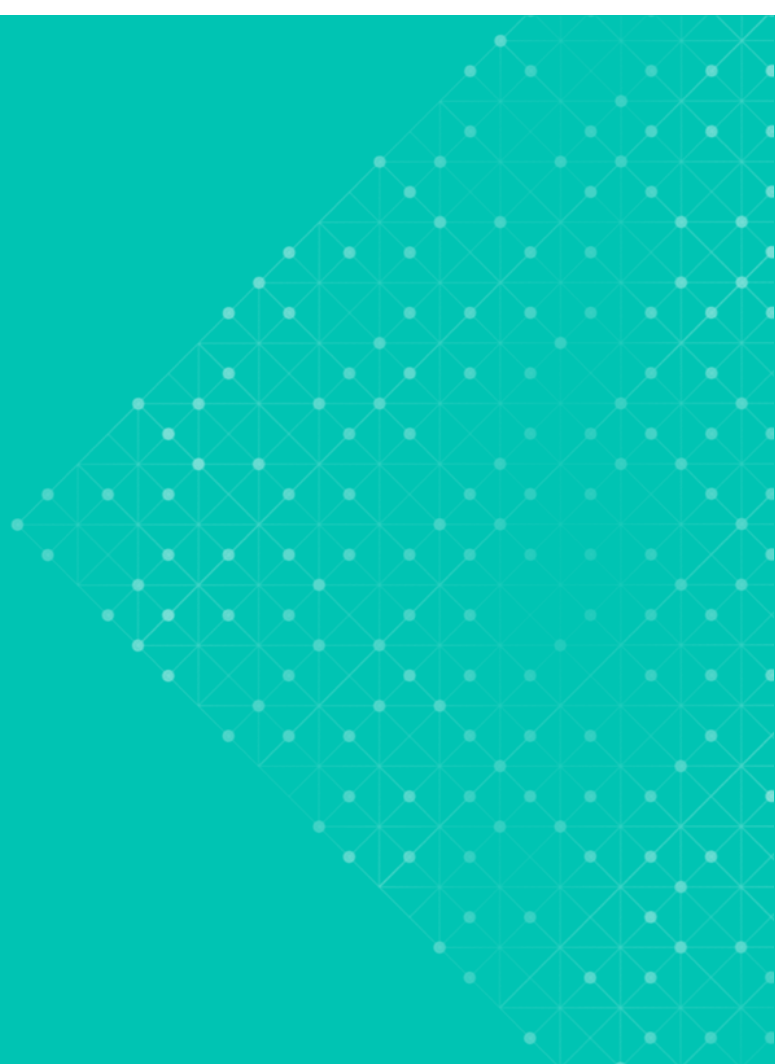
Consultation Questions



Consultation Questions

- **Proposal:** Adjust the targeted decarbonization trajectory of equity CTB/PAB indexes for significant changes to the calculation methodology of GHG intensity as outlined above
 - Do you agree with the proposed default approach to adjust the trajectory to where it would have been, had the new (latest) calculation methodology of GHG Intensity been applied since the original decarbonization start date?
 - Do you agree to implement the default approach in the MSCI EU CTB/PAB Overlay Indexes?
 - Do you agree to implement the default approach in the MSCI Climate Change Indexes?
 - Do you agree to implement the default approach in the MSCI Climate Paris Aligned Indexes?
- **Discussion Point:** MSCI welcomes feedback on customizations of the default approach, which may be appropriate e.g. for specific custom index methodologies, depending on underlying index objectives. Subject to validation on regulatory compliance, such customizations may include:
 - Apply the proposed approach when the decarbonization trajectory needs to be stricter following a methodology change, but remain on the same trajectory if a relaxation would be warranted
 - Apply the proposed approach but calculate the trajectory from a different decarbonization start date

Appendix



Mock-up of Expanded Decarbonization Trajectory Disclosures

Rebalancing date	Decarbonization Start Date	Targeted GHG Intensity ("I") at decarb start date	Years since decarbonization start date ("Y")	Targeted GHG intensity for rebalancing date	Base Date	GHG intensity at the base date
01/06/2020	01/06/2020	100	0	100	01/06/2020	100
...
01/06/2025	01/06/2020	100	5	69.57	01/06/2020	100
01/12/2025	01/06/2020	120	5.5	80.51	01/12/2025	80.51
...
01/12/2027	01/06/2020	120	7.5	69.63	01/12/2025	80.51
01/06/2028	01/06/2020	110	8	61.55	01/06/2028	61.55
01/12/2028	01/06/2020	110	8.5	59.36	01/06/2028	61.55

Significant methodology changes

Fixed start date for 7% y-o-y decarbonization

Adjusted in case of significant methodology changes

$= I * (0.93)^Y$
7% y-o-y reduction since decarb start date

Formal regulatory disclosures: date of latest adjustment & corresponding intensity

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