

# **MSCI Low Carbon SRI Leaders Indexes Methodology**

November 2022

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## 1 Introduction

The MSCI Low Carbon SRI Leaders Indexes<sup>1</sup> (the “Indexes”) are designed to represent the performance of companies that have low carbon transition risk<sup>2</sup> than that of the broad market and have high Environmental, Social and Governance (ESG) performance.

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- MSCI World Low Carbon SRI Leaders Index,
- MSCI USA Low Carbon SRI Leaders Index,
- MSCI Europe Low Carbon SRI Leaders Index,
- MSCI Japan Low Carbon SRI Leaders Index,
- MSCI EM Low Carbon SRI Leaders Index,
- MSCI EMU Low Carbon SRI Leaders Index,
- MSCI China Low Carbon SRI Leaders Index,
- MSCI AC Asia ex Japan Low Carbon SRI Leaders
- MSCI EM EMEA Low Carbon SRI Leaders Index

<sup>2</sup> For details on the Low Carbon Transition Risk, please refer to Appendix 3.

## 2 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 Climate Change Metrics, MSCI ESG Ratings, MSCI ESG Controversies and MSCI ESG Business Involvement Screening Research.

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

### 2.1 MSCI Climate Change Metrics

MSCI Climate Change Metrics provides climate data & tools to support investors integrating climate risk & opportunities into their investment strategy and processes. It supports investors seeking to achieve a range of objectives, including measuring and reporting on climate risk exposure, implementing low carbon and fossil fuel-free strategies, align 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.

For more details on MSCI Climate Change Metrics, please refer to <https://www.msci.com/climate-solutions>

### 2.2 MSCI ESG Ratings

MSCI ESG Ratings provides research, data, analysis and ratings of how well companies manage environmental, social and governance risks and opportunities. MSCI ESG Ratings provides an overall company ESG rating - a seven-point scale from ‘AAA’ to ‘CCC’. In addition, the product provides scores and percentiles indicating how well a company manages each key issue relative to industry peers, as well as underlying data and metrics used to compile the scores and ratings.

The MSCI ESG Ratings methodology can be found in: <https://www.msci.com/esg-and-climate-methodologies>

### 2.3 MSCI ESG Controversies

MSCI ESG Controversies provides assessments of controversies concerning the 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>

## 2.4 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)

### 3 Constructing the MSCI Low Carbon SRI Leaders Indexes

#### 3.1 Defining The Eligible Universe

The eligible universe for the Indexes includes all the constituents of their corresponding market capitalization weighted indexes (the “Parent Index”), as shown in the table below.

Index Name	Parent Index
MSCI World Low Carbon SRI Leaders Index	MSCI World Index
MSCI USA Low Carbon SRI Leaders Index	MSCI USA Index
MSCI Europe Low Carbon SRI Leaders Index	MSCI Europe Index
MSCI Japan Low Carbon SRI Leaders Index	MSCI Japan Index
MSCI EM Low Carbon SRI Leaders Index	MSCI EM Index
MSCI EMU Low Carbon SRI Leaders Index	MSCI EMU Index
MSCI China Low Carbon SRI Leaders Index	MSCI China Index

The eligible securities for the Index are selected from the Parent Index by excluding securities based on the exclusion criteria below:

**Controversial Business Involvement Screens:** Companies that meet the business involvement criteria as defined in section 3.2.1 (Controversial Business Involvement Criteria) of the MSCI SRI Indexes Methodology<sup>3</sup>. In addition to the Controversial Business Involvement Criteria defined in section 3.2.1 of the MSCI SRI Indexes Methodology, the MSCI Low Carbon SRI Leaders Indexes use MSCI ESG Business Involvement Screening Research to identify companies that are involved in the controversial business activities as detailed in Appendix 2.

**Low Carbon Transition (LCT) category<sup>4</sup>:** All companies with Low Carbon transition (LCT) category of Asset Stranding are excluded.

<sup>3</sup> Please refer to the MSCI SRI Indexes methodology at [www.msci.com/index-methodology](http://www.msci.com/index-methodology)

<sup>4</sup> For more details on LCT Category, please refer to Appendix 3.

**Low Carbon Transition (LCT) score<sup>5</sup>:** All companies in bottom 25% of the Parent Index<sup>6</sup> by LCT score are excluded such that cumulative weight of securities remaining in each sector is at least 50% of the weight of the sector in the Parent Index.

### 3.2 Security Selection

Apply MSCI ESG Leaders Indexes Methodology on the Eligible Universe with the following exceptions:

- Companies are required to have an MSCI ESG Rating of ‘BBB’ or above to be eligible for selection.
- Companies should not have faced severe controversies pertaining to Environmental issues.
- Exclusions based on Controversial Business Involvement Criteria as defined in section 3.2.3 of the MSCI ESG Leaders Indexes Methodology<sup>7</sup> are not applied.

After applying MSCI ESG Leaders Indexes methodology, if the Scope 1+2+3 Carbon Emissions Intensity<sup>8</sup> of the Indexes is greater than or equal to 50% of the Scope 1+2+3 Carbon Emissions Intensity of the Parent Index, then the security with the highest Scope 1+2+3 Carbon Emissions Intensity is removed from the Index. This step is repeated till the Scope 1+2+3 Carbon Emissions Intensity of the Indexes is less than 50% of the Scope 1+2+3 Carbon Emissions Intensity of the Parent Index.

### 3.3 Weighting Scheme

The Indexes are constructed by weighting the eligible constituents in proportion of their free float adjusted market capitalization.

The maximum overweight of any issuer in the MSCI Low Carbon SRI Leaders Indexes is capped at 5%. The excess weight of the capped issuers is distributed among the remaining constituents in proportion of their existing weights in the index. After applying issuer capping, if the Scope 1+2+3 Carbon Emissions Intensity of the index is greater than or equal to 50% of the Scope 1+2+3 Carbon Emissions Intensity of the

<sup>5</sup> While applying the LCT score screen, no security with LCT Category of Neutral or Solutions is removed even if these are in the bottom 25% by LCT score. Also, if the sector weight is already less than 50% of the sector weight in the parent index due to earlier screens, then no security will be removed from that sector.

<sup>6</sup> Since, the MSCI ESG Leaders methodology is applied at a regional level, the parent index used in LCT score screen for Europe, EMU, Japan and China is same as the parent index used while applying ESG Leaders Methodology.

<sup>7</sup> Please refer to the MSCI ESG Leaders Indexes methodology at [www.msci.com/index-methodology](http://www.msci.com/index-methodology).

<sup>8</sup> For more details on Carbon Emissions Intensity, please refer to Appendix 5.

Parent Index, then the security with the highest Scope 1+2+3 Carbon Emissions Intensity is removed from the portfolio. This step is repeated till the maximum overweight of any issuer is capped at 5% and the Scope 1+2+3 Carbon Emissions Intensity of the index is less than 50% of the Scope 1+2+3 Carbon Emissions Intensity of the Parent Index.



## 4 Maintaining the MSCI Low Carbon SRI Leaders Indexes

### 4.1 Index Reviews

The Indexes are reviewed on a quarterly basis to coincide with the regular Semi-Annual and Quarterly Index Reviews of the MSCI Global Investable Market Indexes. The changes are generally implemented as of the close of the last business day of February, May, August, and November. The pro forma Index is in general announced nine business days before the effective date.

In general, MSCI uses MSCI ESG Research data (including MSCI ESG Ratings, MSCI ESG Controversies Scores and MSCI Business Involvement Screening Research) as of the end of the month preceding the Index Reviews for the rebalancing of the MSCI ESG Leaders Indexes. For some securities, such data may not be published by MSCI ESG Research by the end of the month preceding the Index Review. For such securities, MSCI will use ESG data published after the end of month, when available, for the rebalancing of the MSCI ESG Leaders Indexes.

### 4.2 Ongoing Event Related Changes

The general treatment of corporate events in the MSCI Low Carbon SRI Leaders 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.

The following section briefly describes the treatment of common corporate events within the MSCI Low Carbon SRI Leaders Indexes.

No new securities will be added (except where noted below) to the Index between Index Reviews. For cases where additions are noted below, securities will be added to the index only if added to the parent index. 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 not be added to the

Index at the time of event implementation.

**Merger/Acquisition**

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.

For Mergers and Acquisitions, 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.

The MSCI Corporate Events methodology book is available at:  
<https://www.msci.com/index-methodology>.

## Appendix 1 : MSCI China Low Carbon SRI Leaders Capped Index

The MSCI China Low Carbon SRI Leaders Capped Index is created on top of the MSCI China Low Carbon SRI Leaders Index by capping the maximum weight of any issuer in the MSCI China Low Carbon SRI Leaders Index at 18% in accordance with the MSCI Capped Indexes methodology<sup>9</sup>. The excess weight of the capped issuers is distributed among the remaining constituents in proportion of their existing weights in the index.

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<sup>9</sup> Please refer to the MSCI Capped Indexes methodology at [www.msci.com/index-methodology](http://www.msci.com/index-methodology).

## Appendix 2: Controversial Business Involvement Criteria

In addition to the Controversial Business Involvement Criteria defined in section 3.2.1 of the MSCI SRI Indexes Methodology, the MSCI Low Carbon SRI Leaders Indexes use MSCI ESG Business Involvement Screening Research to identify companies that are involved in the controversial business activities detailed below:

- **Controversial Weapons**
  - 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 Global Ex-Controversial Weapons.
- **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 deriving 10% or more aggregate revenue from the production, distribution, retail, supply and licensing of tobacco-related products

- **Thermal Coal**
  - All companies deriving 10% or more revenue (either reported or estimated) from thermal coal mining.
  - All companies generating 10% or more power from thermal coal
  - All companies with 10% or more installed capacity for thermal coal
  - All companies deriving 10% or more revenue from thermal coal-based power generation
- **Nuclear Power**
  - All companies generating 30% or more of their total electricity from nuclear power in a given year
  - All companies that have 30% or more of their installed capacity attributed to nuclear sources in a given year
  - All companies deriving 30% or more revenue (either reported or estimated) from the ownership or operation of nuclear power plants
- **Oil and Gas**
  - All companies deriving any revenue from unconventional oil and gas (including revenue from arctic oil and gas).
  - All companies deriving 5% or more revenue from oil and gas related activities, including pipelines and transportation, refining and equipment and services.
- **Weapons**
  - All companies deriving 5% or more revenue from weapons systems, components, and support systems and services
- **Conventional Oil & Gas Extraction**
  - All companies deriving any revenue (either reported or estimated) from conventional oil and gas production. It includes revenue from the production of deepwater, shallow water, and other onshore/offshore oil and gas. It excludes revenue from unconventional oil and gas production (oil sands, shale oil, shale gas) and onshore/offshore oil and gas production in the Arctic region
- **Oil & Gas-based Power Generation**
  - All companies generating more than 30% of their total electricity from liquid fuel and natural gas in a given year

- All companies that have more than 30% of installed capacity attributed to liquid fuel and natural gas in a given year
- All companies deriving more than 30% revenue (either reported or estimated) from liquid fuel- and natural gas-based power generation
- **Fossil Fuel and Nuclear Energy based Power Generation<sup>10</sup>**
  - All companies deriving any revenue from Fossil Fuel based or Nuclear energy based Power Generation.
  - All companies deriving 50% or more revenue from nuclear power activities.
- **United Nations Global Compact Principles:**
  - All companies which are unrated on United Nations Global Compact Principles compliance.

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<sup>10</sup> Such companies, where the total revenue derived from any of the six environmental impact themes including alternative energy, energy efficiency, green building, pollution prevention, sustainable water, or sustainable agriculture is greater than or equal to 50, are exempted from this screen. Similarly, companies with one or more active carbon emissions reduction target/s approved by the Science Based Targets initiative (SBTi) are exempted from this screen.



## Appendix 4: MSCI Low Carbon SRI Leaders Capped Indexes

The MSCI AC Asia ex Japan Low Carbon SRI Leaders Capped Index, MSCI EM LATAM Low Carbon SRI Leaders Capped Index, and MSCI EM EMEA Low Carbon SRI Leaders Capped Index (herein, “MSCI Low Carbon SRI Leaders Capped Indexes”) are designed to represent the performance of companies that have low carbon exposure than that of the broad market and have high Environmental, Social and Governance (ESG) performance. The Indexes are free float-adjusted market capitalization weighted.

### Eligible Universe

The eligible universe for MSCI Low Carbon SRI Leaders Capped Indexes includes all the constituents of their respective MSCI parent index (the “Parent Index”), as shown in the table below.

Index Name	Parent Index
MSCI AC Asia ex Japan Low Carbon SRI Leaders Index	MSCI AC Asia ex Japan Index
MSCI EM LATAM Low Carbon SRI Leaders Index	MSCI EM LATAM Index
MSCI EM EMEA Low Carbon SRI Leaders Index	MSCI EM EMEA Index

### Selecting Companies with The Lowest Carbon Exposure And Highest ESG Performance

The two rules described below are applied independently, and securities selected by both rules are eligible for inclusion in the index.

#### Lowest Carbon Exposure Selection Rules

From the securities in the eligible universe, companies with low exposure to carbon risk, identified as companies with low carbon emission intensity and low potential emissions per dollar of market capitalization, are selected for inclusion in the index.

The Parent Index constituents are ranked by their carbon emission intensity, and the top 20% of securities are excluded from the Index. The cumulative weight of securities excluded from any sector of the Parent Index has a limit of 30%. If the limit is reached for any sector, no further securities from that sector are excluded.



The Parent Index constituents are ranked by their potential emissions per dollar of market capitalization. Securities are excluded until the cumulative potential carbon emission of the excluded securities reaches 50% of the Parent Index.

The two screens mentioned above are applied independently.

### Highest ESG Performance Selection Rules

The MSCI ESG Leaders Indexes Methodology<sup>12</sup>, using the Controversial Business Involvement Criteria, as defined in section 3.2.1 (Controversial Business Involvement Criteria) of the MSCI SRI Indexes Methodology<sup>13</sup>, instead of the Controversial Business Involvement Criteria used in the MSCI ESG Leaders Indexes Methodology, is applied on the eligible universe to select the securities with the highest ESG Performance.

In addition to the Controversial Business Involvement Criteria defined in section 3.2.1 of the MSCI SRI Indexes Methodology, the MSCI Low Carbon SRI Leaders Indexes use MSCI ESG Business Involvement Screening Research to identify companies that are involved in the controversial business activities as detailed below:

- Weapons
  - All companies deriving 10% or more revenue from weapons systems, components, and support systems and services
- Conventional Oil & Gas Extraction
  - All companies deriving any revenue (either reported or estimated) from conventional oil and gas production. It includes revenue from the production of deepwater, shallow water, and other onshore/offshore oil and gas. It excludes revenue from unconventional oil and gas production (oil sands, shale oil, shale gas) and onshore/offshore oil and gas production in the Arctic region
  - Oil & Gas-based Power Generation
    - All companies generating more than 30% of their total electricity from liquid fuel and natural gas in a given year
    - All companies that have more than 30% of installed capacity attributed to liquid fuel and natural gas in a given year
    - All companies deriving more than 30% revenue (either reported or estimated) from liquid fuel- and natural gas-based power generation

<sup>12</sup> Please refer to the MSCI ESG Leaders Indexes methodology at [www.msci.com/index-methodology](http://www.msci.com/index-methodology).

<sup>13</sup> SRI Indexes methodology at [www.msci.com/index-methodology](http://www.msci.com/index-methodology)

- United Nations Global Compact Principles:
  - All companies which are unrated on United Nations Global Compact Principles compliance

### Weighting Scheme

The MSCI Low Carbon SRI Leaders Capped Indexes are constructed by weighting the eligible constituents in proportion of their free-float adjusted market capitalization.

The maximum weight of any issuer in the MSCI Low Carbon SRI Leaders Capped Indexes is capped at a predetermined level in accordance with the MSCI Capped Indexes methodology<sup>14</sup>. The excess weight of the capped issuers is distributed among the remaining constituents in proportion of their existing weights in the index.

Index Name	Issuer Level Capping
MSCI AC Asia ex Japan Low Carbon SRI Leaders Capped Index	10% <sup>15</sup>
MSCI EM EMEA Low Carbon SRI Leaders Capped Index	18%
MSCI EM LATAM Low Carbon SRI Leaders Capped Index	18%

In addition to the issuer level capping for MSCI AC Asia ex Japan Low Carbon SRI Leaders Capped Index, a country level cap is applied for securities in India, further details in Appendix 5.

<sup>14</sup> For more details, please refer to the Capped Indexes methodology at [www.msci.com/index-methodology](http://www.msci.com/index-methodology).

<sup>15</sup> The issuer level capping may not apply for India, given the capping is applied at the country level. Further details in Appendix 5.

## Appendix 5: MSCI AC ex Japan Low Carbon SRI Leaders Capped Index

The maximum weight of India in the MSCI AC Asia ex Japan Low Carbon SRI Leaders Capped Index is capped<sup>16</sup> at 20%. A buffer of 10% of the capping threshold (2%) is used to reduce the risk of non-compliance due to short term market movements between two quarterly rebalances.

A monthly check on securities in India will be applied, such that if the weight of securities in India exceeds 20%, the Index will be reweighted. The excess weight will be distributed among the remaining constituents in proportion of their existing weights in the index.

The monthly check is only applied for the country level capping in India.

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<sup>16</sup> For more details, please refer to the Capped Indexes methodology at [www.msci.com/index-methodology](http://www.msci.com/index-methodology).

## Appendix 6: Calculation of Carbon Emissions Intensity

For Parent Index constituents where the Scope 1+2+3 Emissions Intensity is not available, the average Scope 1+2+3 Emissions Intensity of all the constituents of the MSCI ACWI in the same GICS Industry Group in which the constituent belongs is used.

Security Level Carbon Emissions Intensity =

$$\frac{\text{Scope 1 + 2 + 3 Carbon Emissions}}{\text{Enterprise Value + Cash(in M\$)}}$$

**The following sections have been modified since January 2018:**

Update to include the index construction parameters for the MSCI EM Low Carbon SRI Leaders Index

**The following sections have been modified since March 2018:**

Update to include the index construction parameters for MSCI AC Asia ex Japan Low Carbon SRI Leaders Index and the MSCI AC Asia ex Japan Low Carbon SRI Leaders 10% Capped Index.

**The following sections have been modified since January 2019:**

Update to include:

- The enhanced value business exclusions from the MSCI SRI Indexes methodology
- The updated index names from the MSCI ESG Leaders Low Carbon ex Tobacco Involvement 5% Indexes to the MSCI Low Carbon SRI Indexes

**The following sections have been modified since May 2020:**

Update to include the index construction parameters for the MSCI EMU Low Carbon SRI Leaders Index

**The following sections have been modified since June 2020:**

Update to include the index construction parameters for the MSCI China Low Carbon SRI Leaders Index and the MSCI China Low Carbon SRI Leaders 18% Issuer Capped Index

**The following sections have been modified since August 2020:**

Update to include the index construction parameters for the MSCI EM EMEA Low Carbon SRI Leaders Index, MSCI EM LATAM Low Carbon SRI Leaders Index, MSCI EM EMEA Low Carbon SRI Leaders 18% Issuer Capped Index and MSCI EM LATAM Low Carbon SRI Leaders 18% Issuer Capped Index

**The following sections have been modified since December 2020:**

- Section 2.2.2  
Updated to reflect additional Controversial Business Involvement Criteria  
Appendix 1  
Updated to reflect new branding of the MSCI Low Carbon SRI Leaders Capped Indexes

- Appendix 2  
Updated to reflect detailed description of the additional Controversial Business Involvement Criteria

**The following sections have been modified since December 2020:**

- Section 2.2.2  
Updated to reflect additional Controversial Business Involvement Criteria
- Appendix 1  
Updated to reflect new branding of the MSCI Low Carbon SRI Leaders Capped Indexes
- Appendix 2  
Updated to reflect detailed description of the additional Controversial Business Involvement Criteria

**The following sections have been modified since May 2022:**

- Section 2.1, 2.2, 2.3 and 2.4 to incorporate changes in methodology
- Appendix 2 to include additional screening criteria
- Appendix 3 to include MSCI Low Carbon Transition Assessment
- Appendix 4 to include the methodology of MSCI Low Carbon SRI Leaders Capped Indexes.

**The following sections have been modified since November 2022:**

- Section 2 added to show ESG Research Products used
- Appendix 5 to reflect the country level capping in India and the monthly check to ensure securities in India remain below 20% at the beginning of the month.

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