MSCI Announces Results of the 2014 Annual Market Classification Review

Geneva – June 10, 2014 – MSCI Inc. (NYSE: MSCI), a leading provider of indexes and other investment decision support tools worldwide, announced today that China A-shares will not be included in the MSCI Emerging Markets Index as part of the 2014 Annual Market Classification Review, but will remain on the review list as part of the 2015 Annual Market Classification Review.

This decision is based on feedback highlighting remaining investability constraints linked to the QFII and RQFII quota systems received from international institutional investors in a consultation launched in March 2014 on a potential roadmap for inclusion of China A-shares in the MSCI China and MSCI Emerging Markets Indexes. Because of the significant size of the China A-shares market, the possibility of further regulatory reforms and other changes expected in the near term, such as implementation of the Shanghai/Hong Kong Stock Connect program, MSCI believes that it is important to continue to engage with the international investment community on the potential inclusion of the China A-shares in Emerging Markets as part of the 2015 Annual Market Classification Review.

To provide additional tools for international investors investing in the China A-share market, MSCI will introduce by June 27, 2014, the MSCI China A International Index as a standalone index constructed using the MSCI Global Investable Market Index methodology. This index and the associated regional and global combinations can be used as benchmarks by global investors with QFII and RQFII allocations to complement the already extensive series of MSCI China A Indexes.

“Many international investors are already investing in the China A-share market and the amount of quota granted has increased significantly over the past two years,” said Remy Briand, MSCI Managing Director and Head of Index Research. “So the A-share market is effectively opening as we speak. MSCI’s role is to reflect in its indexes the increasing opportunity set as it occurs. Feedback from investors through this consultation is that they are generally supportive of an inclusion into the index over time but the current quota is still too constraining to warrant an inclusion in the mainstream index right now. We will keep the China A-shares on the list for potential inclusion into Emerging Markets and closely monitor the development of various schemes, such as the Shanghai/Hong Kong Stock Connect program, as they are implemented and used by investors.”

MSCI also announced today that the MSCI Korea and MSCI Taiwan indexes will be removed from the review list of country indexes proposed for potential reclassification to Developed Markets. This decision is motivated by the absence of any significant improvements in key areas negatively affecting accessibility in the Korean and Taiwanese equity markets for the past few years. Both indexes may be added back to the review list as soon as there will be meaningful improvements.

MSCI continues to closely monitor the ongoing tensions between Ukraine and Russia. In the case of a potential material deterioration of the situation resulting in restrictions on the accessibility of the Russian and/or Ukrainian equity markets due to introduction of restrictive measures, such as third party economic sanctions or capital or foreign exchange controls, MSCI may launch a public consultation on the treatment of the MSCI Russia and/or MSCI Ukraine Indexes in the MSCI Global Investable Market Indexes.

Following the substantial increase in Egyptian foreign currency reserves, MSCI also announced that it is no longer considering launching a public consultation on a potential exclusion of the MSCI Egypt Index from the MSCI Emerging Markets Index.

Finally, MSCI also released today the 2014 Global Market Accessibility Review for the 82 markets it covers. The classification of markets is a key part of the process of index construction because it drives the composition of the investment opportunity sets to be represented. The approach used by MSCI aims to reflect the views and practices of the international investment community by striking a balance between a country's development and the accessibility of its market while preserving index stability.

MSCI conducts an annual review of all countries included in the MSCI indexes to ensure that they continue to reflect the standards of the underlying market classification. Results of annual reviews are announced each June.

Once MSCI determines, based on its market classification framework, that a given market may qualify for potential reclassification, it will be added to the list of markets under review. MSCI may then launch a public consultation on the proposed reclassification to gather views from the investment community.

MSCI may also remove a market from the review list if the reclassification proposal has not been endorsed by international investors for several consecutive years due to inadequate progress in market accessibility levels.

Markets Remaining on the Review List

1) **Potential Inclusion in Emerging Markets**

China A: China A-shares will remain under review for a potential partial inclusion in the MSCI China and MSCI Emerging Markets Indexes as part of the 2015 Annual Market Classification Review.

MSCI has received mixed feedback from the investment community regarding the potential partial inclusion in the MSCI Emerging Markets Index. On the one hand, a significant number of the investors who were consulted would welcome the inclusion of China A-shares and regard the partial inclusion of A-shares in the MSCI global indexes as a natural reflection of the current level of market opening. On the other hand, a majority of investors view inclusion as premature because the current QFII and RQFII quota systems are seen as restrictive and as offering uneven levels of market access. In addition, some investors find it challenging to operate under multiple access regimes characterized by different levels of restrictions.

One of the main issues under the current system is that not all investors are offered a fair level of market access based on their asset size, location of operation, investor profile, investment type and the chosen access scheme. For example, the one billion US dollar individual quota cap under the current QFII scheme affects large international passive asset managers more severely than other investors because it fails to accommodate the necessary investment allocation to track the MSCI Emerging Markets Index based on the assets under management of a large passive asset manager. Some smaller investors may also find the QFII scheme challenging, in their case because qualifying for the scheme or applying only for a small quota required to match the potential benchmark allocation may be difficult.

In addition, the current limited eligible locations under the RQFII scheme mean that investors outside Hong Kong, Singapore, London and Paris may not be able to access the China A-share market via this scheme.

Market accessibility issues highlighted during the consultation continue to surround a) allocation of quotas, b) limitation on capital mobility and c) uncertainty regarding the applicable capital gains tax.

- On quota allocation, apart from the lack of alignment between quota allocation and the size of investors, the presence of an approval process and the uncertainty of gaining additional quota on a timely basis make it difficult for market participants to operate within the normal investment process. In addition, the lack of flexibility to deploy QFII quota freely across different investment accounts and investment types (such as open-ended funds versus segregated accounts) makes it challenging for some investors to efficiently utilize the quota within or across the wider organization.

- With respect to capital mobility limitations, the existence of capital remittance and lock-up periods continues to be a concern to a large number of investors because they limit flexibility in deploying capital in accordance with investment views. Capital repatriation is also viewed as problematic because repatriation frequency varies among daily under RQFII, weekly for QFII open-ended funds and monthly for others, creating frictions from a fund/investment operation perspective. Some market participants also question the ability to promptly repatriate investment proceeds should the need arise.

- Uncertainty around the application of the capital gains tax is also a problem for some investors. The need for setting aside capital gains tax provision and its resulting effects on tracking error and profit repatriation are frequently highlighted as a concern by investors. While some market participants have chosen to make no tax provision, some investors perceive the lack of tax clarity a major compliance and operational risk.

In addition to the above, a number of additional market accessibility issues were identified:

- Questionable best trade execution due to the difficulty in using multiple brokers
- Potential need for pre-funding due to the short settlement cycle
- No same-day turnaround trade
- Inability to trade at Shanghai Stock Exchange market close for passive investors
- Uncertainty over legal ownership and its potential fiduciary implications due the lack of real nominee structure

One development warranting further review is the recently announced Shanghai/Hong Kong Stock Connect program, which, although not yet implemented, could potentially represent an important market development. Its announcement has so far received some preliminary positive feedback from international institutional investors. Some view this new program as an access channel that has the potential to mitigate some of the market accessibility issues posed by the current QFII/RQFII systems. However, time will be needed for the scheme to become fully operational, and then investors will need to gain actual investment experience before the program can be meaningfully evaluated. MSCI will be actively monitoring the overall accessibility level of A-shares and will continue to seek feedback from the investment community.

Markets Removed from the Review List

1) **Potential Reclassification to Developed Markets**

Korea: MSCI will remove the MSCI Korea Index from the review list for potential reclassification to Developed Markets from the 2015 Annual Market Classification Review. The MSCI Korea Index will be retained in Emerging Markets.

The South Korea equity market continues to meet most of the Developed Markets criteria of the MSCI Market Classification Framework. Notably, economic development, market size and liquidity -- as well as many aspects of the market operational framework -- are at the level of Developed Market standards. There has, however, been a lack of meaningful developments over the past four years with respect to the two accessibility issues highlighted by international institutional investors: the limited convertibility of the Korean Won and the resulting downstream operational inconveniences resulting from the rigidity of the ID system. These two issues are viewed as major misalignments with the current standard for Developed Markets.

The MSCI Korea Index may be added back to the review list for potential reclassification to Developed Markets as soon as there is meaningful progress toward resolution of the above issues.

Taiwan: MSCI will remove the MSCI Taiwan Index from the review list for potential reclassification to Developed Markets from the 2015 Annual Market Classification Review. The MSCI Taiwan Index will be retained in Emerging Markets.

The Taiwan equity market meets many Developed Markets criteria, including those with respect to economic development and market size and liquidity, but several shortcomings on market accessibility continue to prevent the reclassification of the MSCI Taiwan Index to Developed Markets. There has been a lack of meaningful progress over the past four years in resolving a number of issues that are critical to international institutional investors. These important issues continue to be: a) the absence of an offshore currency market for the New Taiwan Dollar, b) the continued existence of prefunding practices in the Taiwanese equity market and c) the rigidity of the ID system that makes the use of in-kind transfers and off-exchange transactions difficult to execute in practice. Similarly, these issues represent major misalignments with the standard for Developed Markets today.

The MSCI Taiwan Index may be added back to the list for potential reclassification to Developed Markets following meaningful progress toward resolution of the above issues.

Other Developments in Markets Not Currently on the Review List

Egypt: The foreign currency reserves in Egypt have substantially increased since the beginning of the year. As a result, the Central Bank of Egypt has fully cleared the backlog of dollars owed to foreign investors seeking to repatriate funds from the country. Based on current information, no new shortage of foreign currency has been reported or is expected to occur in the short term. Consequently, MSCI is no longer considering launching a public consultation on potential exclusion of the MSCI Egypt Index from the MSCI Emerging Market Index.

Global Market Accessibility Review

MSCI released today the results of the 2014 Global Market Accessibility Review, including a year-on-year comparison, for all 82 markets it covers. The Global Market Accessibility Review aims to reflect international investors' experience in investing in a given market and provides a detailed assessment of market accessibility for each country market included in MSCI indexes. In particular, it provides an evaluation of 18 measures in four market accessibility criteria, which are:

- Openness to foreign ownership
- Ease of capital inflows and outflows
- Efficiency of the operational framework
- Stability of the institutional framework

These four criteria reflect the views of international institutional investors, who generally put a strong emphasis on equal treatment of investors, free flow of capital, cost of investment and country-specific risk.

The assessment is intended to serve as the basis for a comparison of countries' market accessibility levels across investment universes. This review also aims to serve as a tool for international institutional investors to better track the evolution of market accessibility in individual countries as well as for regulators to be informed of the areas perceived as not meeting international investor expectations. MSCI welcomes continuous feedback from the investment community on the Global Market Accessibility Review.

The complete results of the 2014 Global Market Accessibility Review, including the detailed assessment of the different market accessibility measures by country, as well as additional information on the MSCI Market Classification Framework and a summary of recent market reclassifications, can be found on MSCI's web site at http://www.msci.com/products/indices/market_classification.html.

MSCI Market Classification Framework

The classification of markets is a key input in the process of index construction because it drives the composition of the investment opportunity sets to be represented. The approach used by MSCI aims to reflect the views and practices of the international investment community by striking a balance between a country's economic development and the accessibility of its market while preserving index stability.

The MSCI Market Classification Framework consists of the following criteria: economic development, size and liquidity and market accessibility.

The economic development criterion is only used in determining the classification of Developed Markets, since it is not relevant between Emerging and Frontier Markets given the very wide variety of economic development levels within each of these two universes.

The size and liquidity requirements are based on the minimum investability requirements for the MSCI Global Standard Indexes. Emerging Markets country indexes with fewer than three companies meeting the Emerging Markets size and liquidity requirements for four consecutive Semi-Annual Index Reviews will be reclassified as Frontier Markets.

Market accessibility aims to reflect international investors' experience in investing in a given market and as a result, this criterion includes several sub-criteria. These criteria are generally based on qualitative measures that are reviewed for all markets at least once a year during the MSCI Global Market Accessibility Review.

MSCI regularly reviews the market classification of all countries included in MSCI indexes to ensure that they continue to reflect the evolution of the different markets. In particular, changes in the assessments under the classification framework serve as the basis for determining the markets that will be reviewed for potential market reclassification as part of the Annual Market Classification Review.

MSCI will only consider markets for upgrade if a change in classification status can be viewed as irreversible. Every June, MSCI communicates its conclusions from the discussions with the investment community on the list of countries under review and announces the new list of countries, if any, under review for potential market reclassification in the upcoming cycle. While adhering to the regular time line for such communication helps provide greater predictability and is less disruptive to a market's normal functioning, MSCI may from time to time exercise prudent discretion and consider off-cycle communications should significant market events take place outside the regular review cycle.

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After posting the review announcement, MSCI will hold two press conference calls in English, hosted by Remy Briand, Managing Director, Global Head of Index and ESG Research, to answer questions from the media. Note that these press conference calls are restricted to journalists.

<u>First Conference Call</u>
Date: Tuesday, June 10, 2014
Time: 11.30pm CEST/10.30pm BST/5.30pm EDT/1.30am GST

Toll Free Numbers:

US: 866-803-2143	Hong Kong: 800-900-592
UK: 0800-279-3953	Japan: 00531-12-1857
China A: 10800-712-1320	China B: 10800-120-1320
S. Korea: 00798-14800-6732	Taiwan: 00801-137-708

Participant passcode: MSCI

<u>Second Conference Call</u>
Date: Wednesday, June 11, 2014
Time: 9.00am CEST/8.00am BST/3.00am EDT/11.00am GST

Toll Free Numbers:

US: 866-803-2143	Hong Kong: 800-900-592
UK: 0800-279-3953	Japan: 00531-12-1857
China A: 10800-712-1320	China B: 10800-120-1320
S. Korea: 00798-14800-6732	Taiwan: 00801-137-708

Participant passcode: MSCI

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About MSCI

MSCI Inc. is a leading provider of investment decision support tools to investors globally, including asset managers, banks, hedge funds and pension funds. MSCI products and services include indexes, portfolio risk and performance analytics, and ESG data and research.

The company's flagship product offerings are: the MSCI indexes with approximately USD 8 trillion estimated to be benchmarked to them on a worldwide basis[1]; Barra multi-asset class factor models, portfolio risk and performance analytics; RiskMetrics multi-asset class market and credit risk analytics; IPD real estate information, indexes and analytics; MSCI ESG (environmental, social and governance) Research screening, analysis and ratings; and FEA valuation models and risk management software for the energy and commodities markets. MSCI is headquartered in New York, with research and commercial offices around the world.

[1]*As of September 30, 2013, as reported on January 31, 2014, by eVestment, Lipper and Bloomberg*

For further information on MSCI, please visit our web site at www.msci.com

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