

Consultation on Implementation Details of a Switch to a Light Rebalancing under Conditions of Market Stress

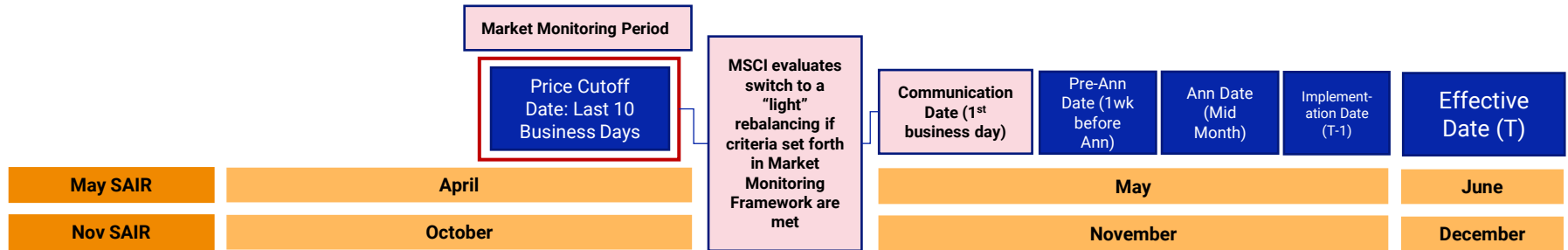
March 2021

Background

- On January 28, 2021, MSCI announced that it will implement the ability to switch a Semi-Annual Index Review (SAIR) to a “light” rebalancing scenario* under conditions of market stress
- While a majority of market participants supported the proposal, many highlighted the importance of transparent and well-defined guidelines for triggering such a scenario, along with a clear communication policy
- Following this feedback, MSCI opens a follow up consultation with proposals around the timeline and criteria for the evaluation of market stress and related public communication
- MSCI welcomes feedback from the investment community until April 2, 2021 and will communicate the results of this consultation by April 16, 2021. Should the proposals be adopted, they will be effective as part of the May 2021 Semi-Annual Index Review
- Clients may provide feedback through an online survey available on:
<http://www.msci.com/index-consultations-light-rebalance>

Summary of the Proposal

- In order to provide transparent and well-defined guidelines for considering a switch to a “light” rebalancing, MSCI proposes to:
 1. Set the “**market monitoring period**” to the last 10 business days of the month preceding the announcement of an index review
 2. Evaluate a potential switch to a “light” rebalancing only when specific criteria set forth in the **MSCI Market Monitoring Framework** are met during the “**market monitoring period**”
 3. Set the “**communication date**” on the decision whether to switch to a “light” rebalancing to the first business day following the market monitoring period if the relevant criteria are met



Triggers for Evaluation of a Switch to a “Light” Rebalancing

- MSCI would consider switching to a “light” rebalancing if either of the below criteria from the MSCI Market Monitoring Framework are met:

(A) Market Liquidity: breach of the following criteria for at least **3 days** within the “market monitoring period”

(1) ACWI volatility breaching **0.55** (approx. 99th percentile of historical observations since 2002)

AND

(2) ACWI bid-ask spread breaching **0.19%** (approx. 99th percentile of historical observations since 2015)

OR

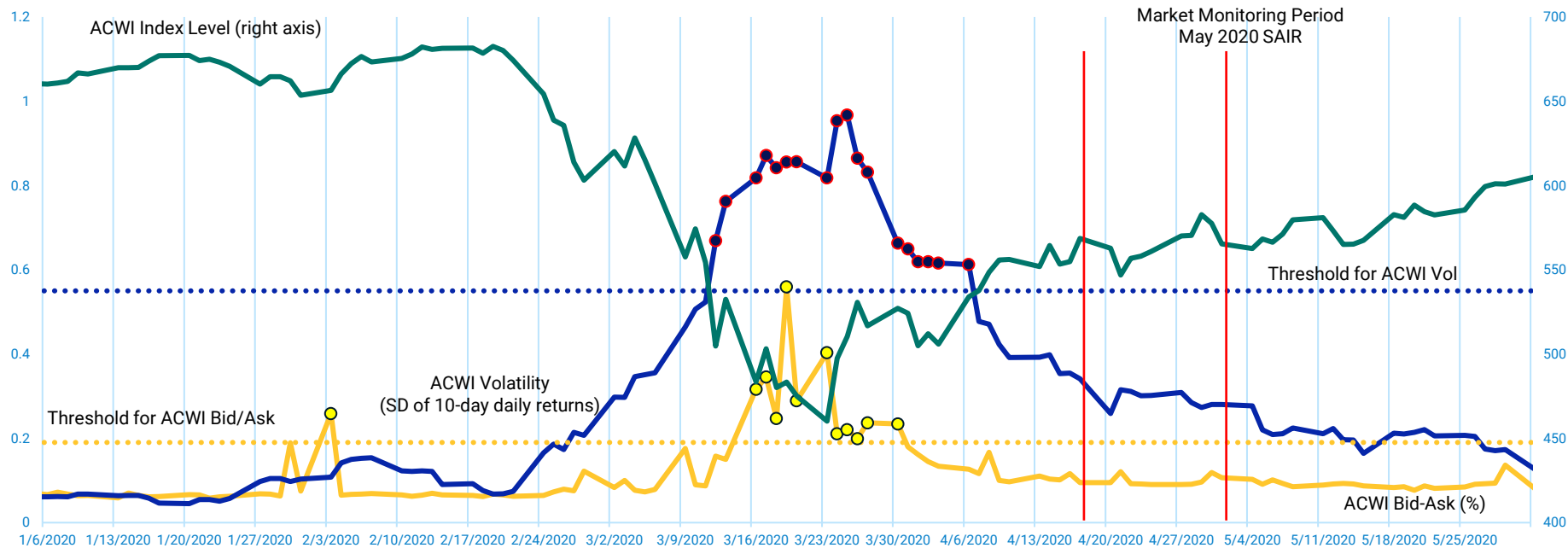
(B) Market Functioning: 20% of the weight of constituents of the MSCI ACWI Index not trading due to full day stock exchange closures, cumulatively within the “market monitoring period”

- MSCI would proceed with the scheduled Semi-Annual Index Review (SAIR) in absence of the above triggers
- If the above criteria are met, a decision on whether switching to a “light” rebalancing is warranted would be taken by the relevant MSCI Index Committees, considering the individual circumstances of the market and trading environment

Proposed Communication Policy

- If the criteria for the evaluation of a switch to a “light” rebalancing are met, MSCI would send a communication on its decision to switch to a “light” rebalancing or not, on or before the first business day after the “**market monitoring period**”
 - There would be no change to the decision to switch or not to switch to a “light” rebalancing following the “**communication date**”
- No communication would be sent if the thresholds for the evaluation of a switch to a “light” rebalancing are not breached during the “**market monitoring period**”
 - MSCI would no longer consider a potential switch to a “light” rebalancing after the “**market monitoring period**” and would proceed with the scheduled SAIR
- Over time, MSCI may review the thresholds used in the MSCI Market Monitoring Framework. Any resulting changes would be made public in the relevant index methodology documentation well in advance of the “**market monitoring period**”

Illustration: May 2020 SAIR

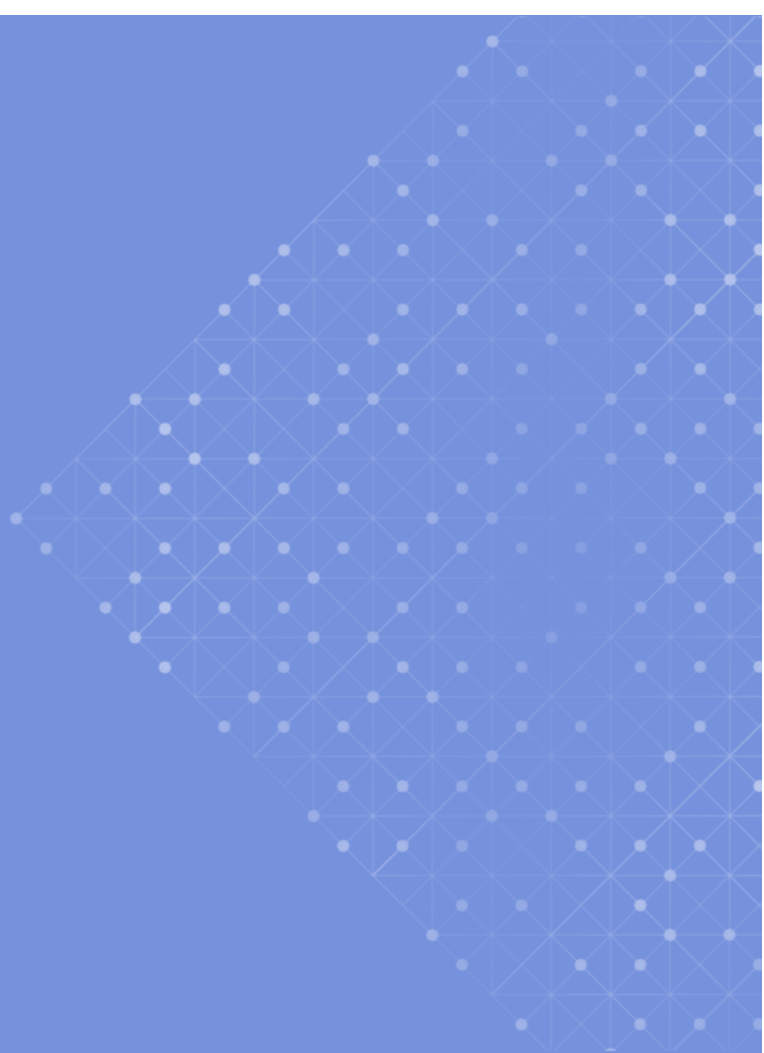


- Under the proposal, MSCI would have implemented the scheduled May 2020 SAIR as none of the criteria were met during the “**market monitoring period**”. The thresholds were breached earlier, during March 2020

Discussion Points

- Do you agree with the proposed length and timeframe of the defined “**market monitoring period**”?
- Does the proposed “**communication date**” provide sufficient lead time prior to the index review implementation?
- Are the proposed **Market Liquidity** measures and thresholds appropriate?
- Is it relevant to consider full day market closures under **Market Functioning** as one of the criteria for evaluating the switch to a “light” rebalancing? Is the proposed threshold appropriate?
- Should partial closures (e.g. caused by circuit breakers) be considered as well?

Appendix



Light Rebalancing for Various Methodologies (Reminder)

- A 'light' rebalancing generally focuses on replacing a scheduled SAIR with a QIR (if such QIR is defined by a methodology)
- If the upcoming scheduled rebalance is already a QIR, then no change to the process would occur
- For methodologies which rebalance annually or where QIRs are not defined, MSCI would proceed as per the normal rebalancing schedule

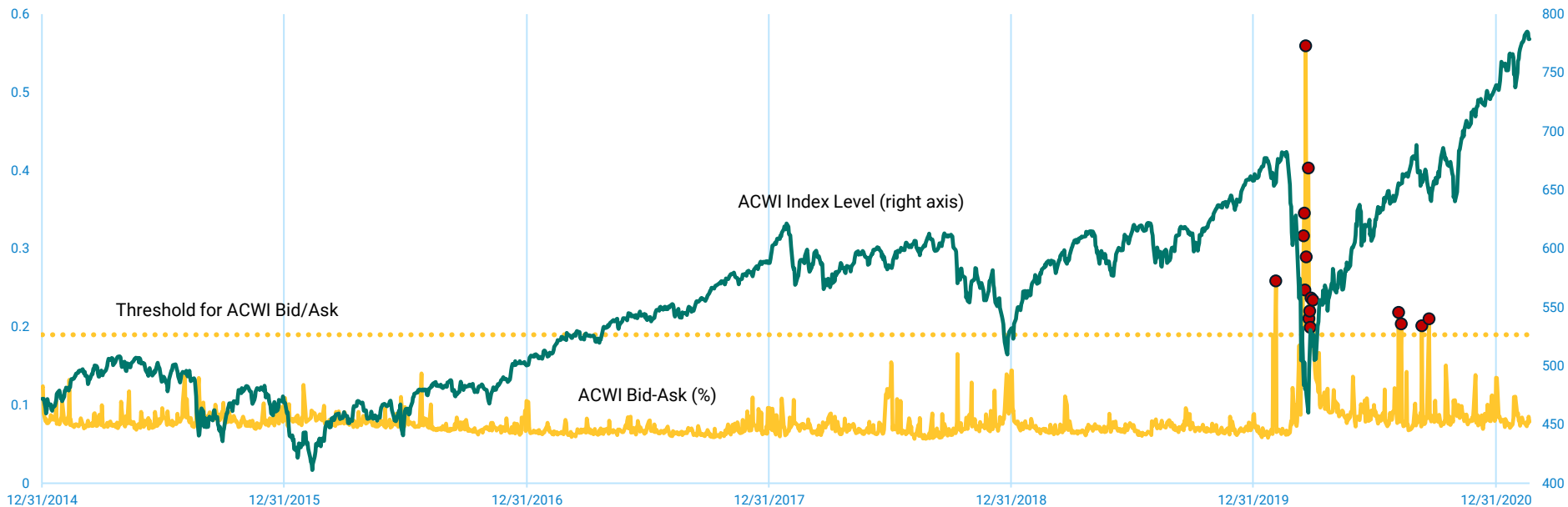
Rebalancing schedules for various methodologies

'Normal' Rebalancing Schedule	Rebalancing schedule during market stress	Index Methodology Example
Semi Annual + QIR	QIR	MSCI Global Investable Market Indexes; MSCI ESG Universal Indexes
Annual only	Annual	MSCI GDP Weighted Indexes
Annual + QIR	Annual	MSCI Top 50 Dividend Indexes
Semi-Annual only	Semi-Annual	MSCI Minimum Volatility Indexes
QIR only	QIR	MSCI Equal Weighted Indexes
Monthly	Monthly	MSCI Hedged Indexes

MSCI Market Monitoring Framework

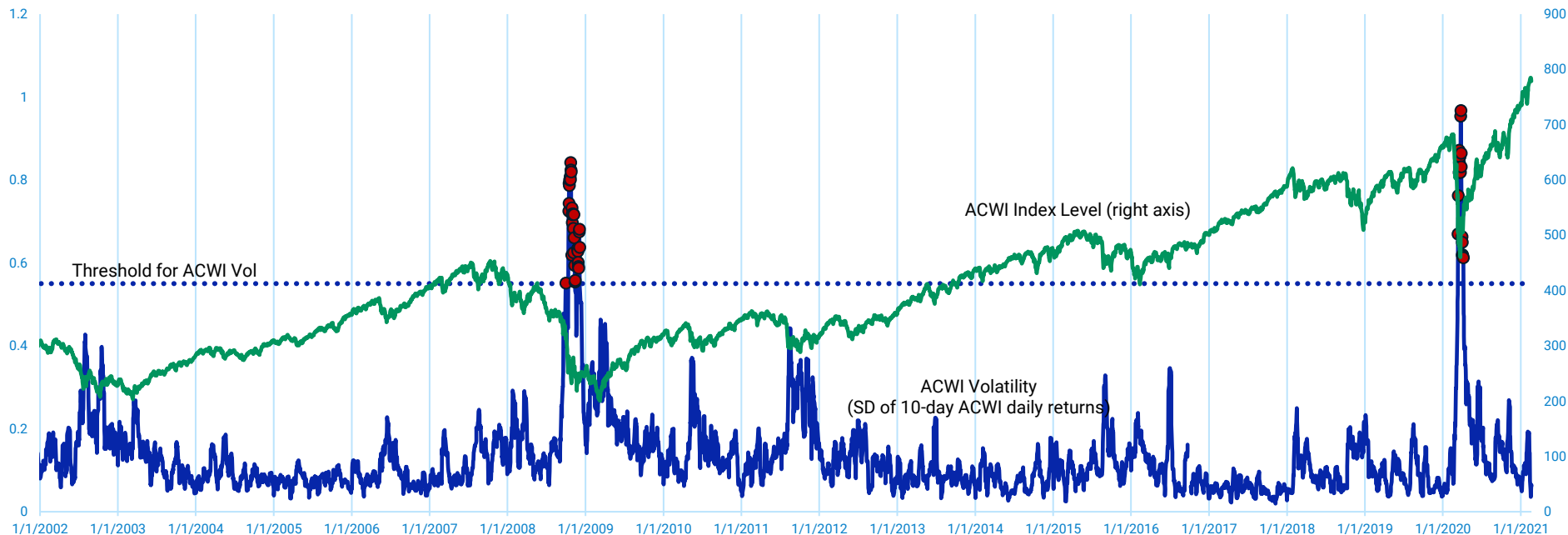
- The **MSCI Market Monitoring Framework** consists of the following three pillars:
 - **Market Liquidity:**
 - ***MSCI ACWI Index Level Bid-Ask spread:*** as an explicit measure of market liquidity
 - Based on the daily MSCI ACWI Index-weighted average bid-ask spread*
 - ***MSCI ACWI Index volatility:*** as an implicit measure of a potential market impact
 - Based on the standard deviation of the rolling 10-day daily returns of the MSCI ACWI Index
 - **Market Functioning:**
 - ***Cumulative weight of constituents of the MSCI ACWI Index*** that are listed on the stock exchanges which are closed for at least one full day due to reasons other than regular market holidays
 - **Data Availability:**
 - Qualitative measure based on the availability of price data inputs for the purpose of the index review

Historical Bid-Ask Spread



- Threshold of 0.19% set based on approximately the 99th percentile of daily ACWI weighted bid-ask spread since 2015

Historical ACWI Volatility



- Threshold of 0.55 set based on approximately the 99th percentile of daily ACWI weighted bid-ask spread since 2002

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