



**Consultation on Potential
Enhancements to the Methodology of
the MSCI GCC Countries Indices**

May 2007

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Summary

The MSCI GCC Countries Indices

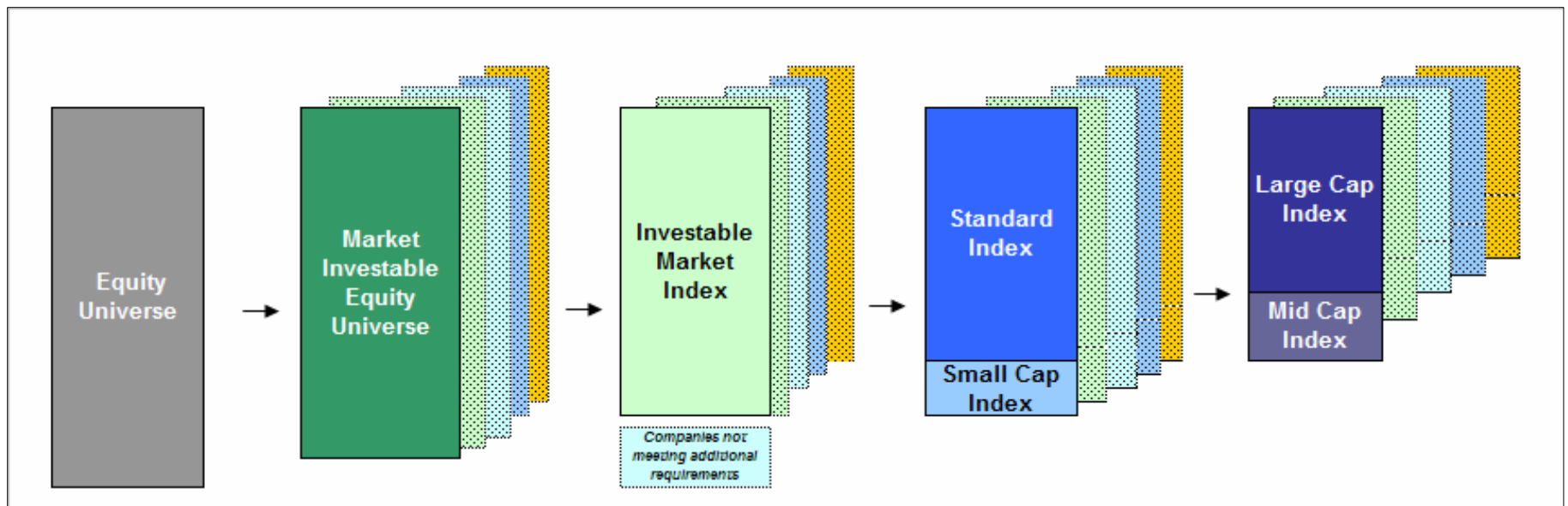
- Please note that the MSCI GCC Countries Indices are standalone indices and therefore are not part of the MSCI Emerging Markets Index
- The MSCI GCC Countries Indices are currently constructed based on a methodology similar to the current MSCI Standard Index Series, targeting for index inclusion 85% of the domestic free float-adjusted market capitalization in each industry group, with minimum size and minimum liquidity requirements by country
 - This sampling approach leads to non-exhaustive coverage, with some sizable companies being excluded
 - In addition, the target 85% coverage of each Industry Group in each market results in a multi-cap index composition
- MSCI Barra is currently consulting on a potential enhancement of the methodology of the MSCI GCC Countries Indices which would target exhaustive representation and non-overlapping size segmentation of the investable universe

Potential Enhancement to the MSCI GCC Countries Indices

- The enhanced GCC Countries Standard Indices would provide exhaustive coverage of the large and mid-cap segments of the universe by targeting a coverage range around 85% of free float-adjusted market capitalization in each market subject to a minimum size range
- New potential GCC Countries Small Cap Indices would target all companies with market capitalization below that of the companies in the enhanced Standard Indices and up to 99% coverage of the free float-adjusted investable universe, subject to minimum investability criteria and a minimum size range
- The enhanced GCC Countries Standard and the new Small Cap Indices would be combined to create a GCC Countries Investable Market Index family with non over-lapping segments, including new Large and Mid Cap size segment indices

Potential Structure of the MSCI GCC Countries Indices

- The proposed structure of the enhanced GCC Countries indices would be as follows



Potential Transition Plan for the MSCI GCC Countries Indices

- The transition would result in additions to the GCC Countries Standard Indices, reclassifications of securities from the GCC Countries Standard Indices to the GCC Countries Small Cap Indices, as well as deletions
- The MSCI GCC Countries Indices would be transitioned in one single phase as of the close of May 30, 2008
- Please note that the potential enhancements discussed in this consultation may or may not be adopted in whole or in part and this consultation may or may not result in any changes to the MSCI GCC Countries Indices



Background

GCC Countries' Markets

- There are six countries in the GCC Countries Indices, each exhibiting different characteristics in terms of market size and liquidity
 - Larger versus smaller markets
 - Liquid versus less liquid markets

Country Universe	Bahrain	Kuwait	Oman	Qatar	Saudi Arabia	United Arab Emirates	GCC Countries
Nb of Companies above USD 5 billion Full Mcap	-	6	-	3	11	9	29
Nb of Companies above USD 5 billion Float Mcap	-	3	-	-	2	1	6
Nb of Companies between USD 5 billion and USD 1 billion Full Mcap	10	20	3	13	28	17	91
Nb of Companies between USD 5 billion and USD 1 billion Free-Float Adjusted Mcap	1	10	-	2	12	6	31
Total Number of Companies	39	164	123	36	87	90	539
Total Country Full Mcap	21,370	148,855	13,549	60,320	308,549	142,776	695,419
Total Country Float Mcap	8,532	64,571	4,534	11,870	69,951	27,708	187,165
Median Annualized Traded Value Ratio (ATVR)	2.0%	51.7%	11.5%	106.6%	1921.0%	6.8%	32.4%
Average Annualized Traded Value Ratio (ATVR)	4.1%	111.7%	80.1%	200.5%	5015.4%	120.5%	895.6%

Note: All market caps are in USD millions. Data as of May 7, 2007

GCC Countries foreign investment restrictions

- The six GCC countries have also more, or less, stringent Foreign Ownership Limits (FOLs) applied to non-domestic investors
 - In Kuwait, Oman, Qatar and the United Arab Emirates the FOLs are currently identical for GCC-based investors and other international investors
 - Saudi Arabia is closed to international non-GCC investors and generally open at 49% to GCC-based investors
 - Bahrain is generally open at 49% to international non-GCC investors and fully open to GCC-based investors

Index Needs and Index Objectives

Investment Process Needs

- The continued evolution of the international equity markets and investment management processes have led investors to desire:
 - Broader coverage of international equity markets while satisfying reasonable investability considerations
 - Size segmentation of the global investable universe and exhaustive coverage of the size segments while satisfying
 - **Size Integrity:** Consistency in defining size cut-offs globally to ensure that companies of comparable and relevant sizes are included in the appropriate size segments
 - **Market Coverage:** Consistency in size segment coverage for each market to allow for country diversification in each segment

- These investment process needs have led to MSCI Barra recent decision to create and implement the Global Investable Market Indices methodology in its international Developed and Emerging Markets Indices

Proposed Index Design Objectives

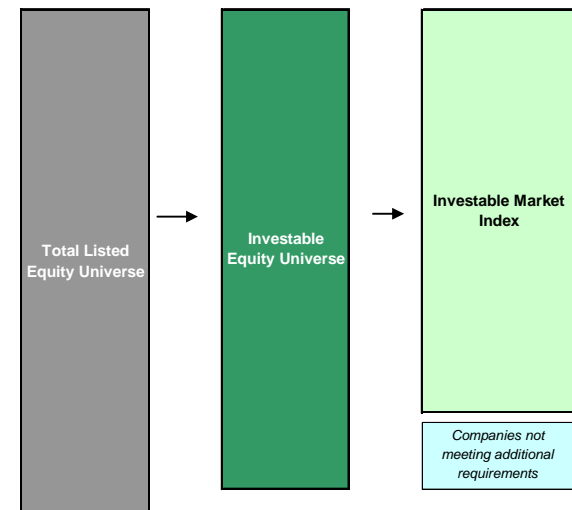
- The key index design objectives for the Global Investable Market Indices are:
 - A balance between investability and market coverage needs to be achieved
 - Investability is more important than complete coverage of the universe in each market
 - Size integrity, market coverage, and index stability are the appropriate objectives for size segment indices
 - Balancing those three objectives, rather than fully achieving one at the expense of the other two, is preferred
 - When a balance cannot be achieved, some sacrifice in country coverage and representation is acceptable to preserve size integrity

- Are these investment needs and index design objectives also relevant for the MSCI GCC Countries Indices?

Methodology Proposal

Methodology Proposal: Deriving the Investable Universe

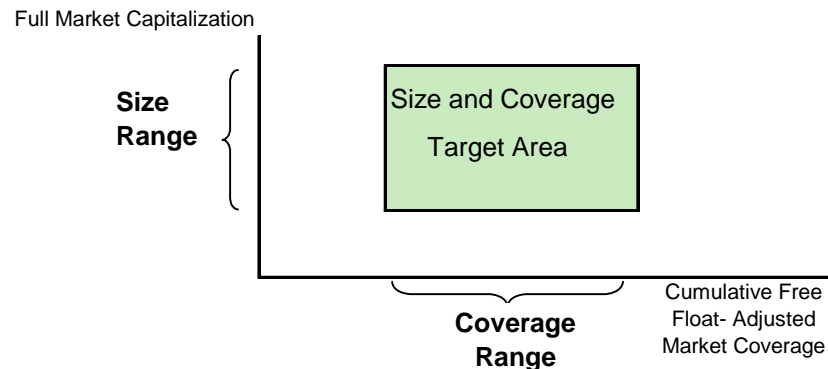
- Investability screens are used to arrive at an investable universe and the Investable Market Index to ensure replicability of constituents
- Equity Universe Minimum Size Requirements: Different levels are needed to account for the different size structure among the GCC Countries markets (as of April 12, 2007, in full market capitalization)
 - Larger markets: Kuwait, Saudi Arabia and the United Arab Emirates – Minimum USD 156 mm
 - Smaller markets: Bahrain, Oman and Qatar – Minimum USD 78 mm
- Equity Universe Free Float-Adjusted Capitalization Requirement
 - 50% of the Equity Universe Minimum Size Requirement
- Different levels of liquidity need to be determined in order to account for the specific market characteristics of the six GCC Countries
 - More liquid markets: Kuwait, Oman, Qatar and Saudi Arabia – Minimum 15% ATVR
 - Less liquid markets: Bahrain and the United Arab Emirates – Minimum 5% ATVR
- Global Minimum FIF Requirement: 0.15 – in general
- Minimum 3 months of Trading Requirement – in general



Methodology Proposal: Constructing Appropriate Size Segments

Deriving the Size and Coverage Target Area

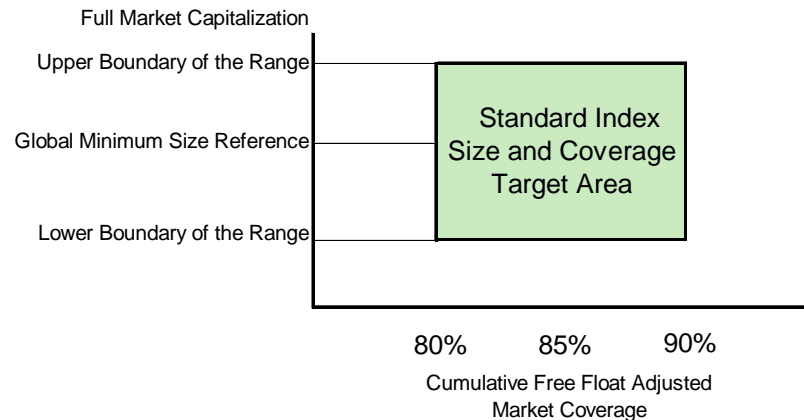
- The distribution of company market capitalizations varies from market to market. Therefore the use of the same company size cut-offs and the same market coverage targets to create size segments is not feasible
- Striking a balance between size integrity and market coverage requires the use of :
 - Global minimum company size **ranges**, and
 - Market coverage target **ranges**
- The intersection of the minimum size range with the coverage range describes a Size and Coverage Target Area which will be used to find a balance between size integrity and market coverage



Methodology Proposal: Constructing Appropriate Size Segments (cont'd)

Defining Coverage and Size Ranges

- The market coverage range proposed for various segments is defined as coverage of:
 - 65% to 75% in each market for the Large Cap Index
 - 80% to 90% in each market for the Standard Index and
 - 98.5% to 100% in each market for the Investable Market Index
- The global minimum company size range for each segment is defined by:
 - First determining a global minimum size reference and
 - Then specifying a range around the global minimum size reference



Methodology Proposal: Global Minimum Size reference options

- There are two different options to determine the global minimum size references for the GCC countries
 - Option 1: Base the global minimum size reference on the GCC countries universe
 - Option 2: Link the global minimum size references to the EM global minimum size reference
- MSCI Barra proposes to use option 2 in view of the following benefits:
 - Higher stability of a reference based on a broad universe
 - Compatibility with the MSCI Global Investable Market Indices Methodology that MSCI has decided to implement for its Developed and Emerging Markets Indices

Methodology Proposal: Global Minimum Size Reference

- The global minimum size references for the size segment indices are derived by:
 - First aggregating the individual Developed Market countries investable universes to create a global investable universe
 - Then choosing the full market capitalization at:
 - The 70th percentile as the cut-off between the Large Cap and Mid Cap Index
 - The 85th percentile as the cut-off for the Standard Index, i.e., between the Mid Cap and Small Cap Index
 - The 99th percentile as the cut-off at the bottom for the Investable Market Index
- For Emerging Markets, the global minimum size reference is set at ½ the level of the Developed Markets

Percent of Free Float Adjusted Market Coverage	Developed Markets Investable Equity Universe	Developed Markets Full Market Capitalization	Emerging Markets Full Market Capitalization (50% of DM)
70%	Large Cap	11,964	5,982
85%	Mid Cap	4,062	2,031
99%	Small Cap	370	185

Data as of April 12

Methodology Proposal: Minimum Size Ranges

- Two different types of ranges are required to accommodate for the very different size structures among the GCC Countries

– Larger GCC Countries

- The Global Minimum Size Range for each size segment would be identical to the Emerging Markets Global Minimum Size Range (1.15 times to 0.5 times the Emerging Markets Global Minimum Size Reference)

– Smaller GCC Countries

- The Global Minimum Size Range for each size segment would be determined by specifying a broader range of 0.25 times to 1.15 times half of the Emerging Markets Global Minimum Size Reference

Segment Size and Coverage Target Area

Larger Countries		Smaller Countries	
1.15x = USD 6,879 million	Large Cap	1.15x = USD 3,440 million	75%
0.5x = USD 2,991 million		0.25x = USD 748 million	
	65%		
1.15x = USD 2,246 million	Mid Cap	1.15x = USD 1,168 million	90%
0.5x = USD 1,016 million		0.25x = USD 254 million	
	80%		
1.15x = USD 213 million	Small Cap	1.15x = USD 106 million	100%
0.5x = USD 93 million		0.25x = USD 23 million	
	98.5%		

Data as of April 12, 2007

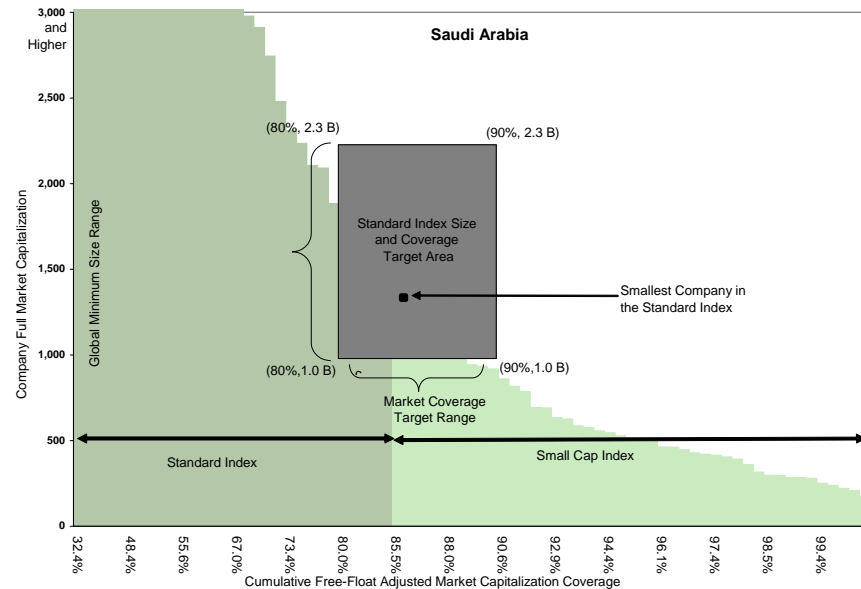
Methodology Proposal: Balancing Size Integrity & Market Coverage

- Size integrity is achieved when the market capitalization of the smallest company in the segment within a market falls within the company minimum size range
- Adequate country representation is achieved when the cumulative market coverage of the investable universe falls within the coverage target range
- Achieving a balance between size integrity and market coverage requires that both size integrity and country coverage are achieved
 - However, in some instances this is not possible and country coverage is allowed to deviate from the target coverage band in order to achieve size integrity
- At initial construction the number of companies is chosen to balance both objectives and the market capitalization of the smallest company becomes the minimum size cut-off for that market

Enhanced GCC Countries Standard Index

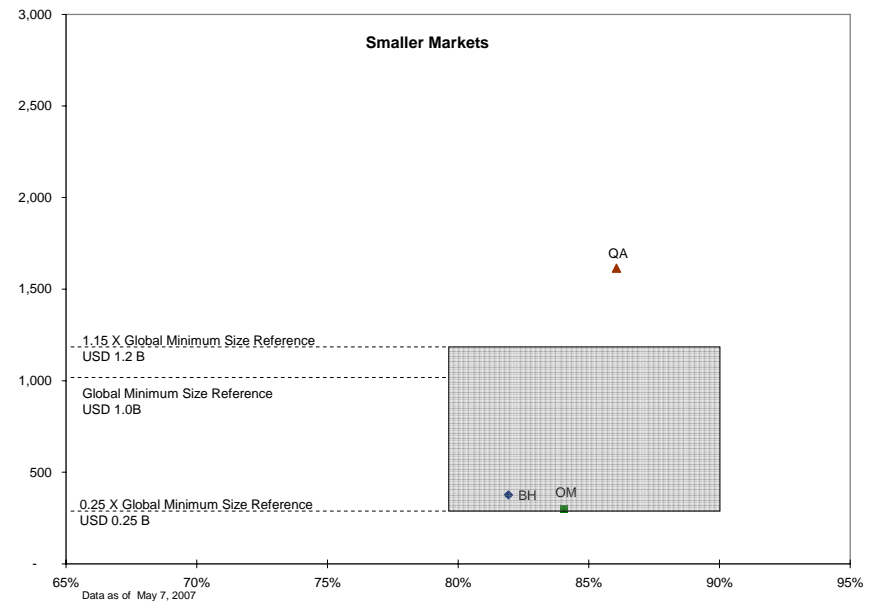
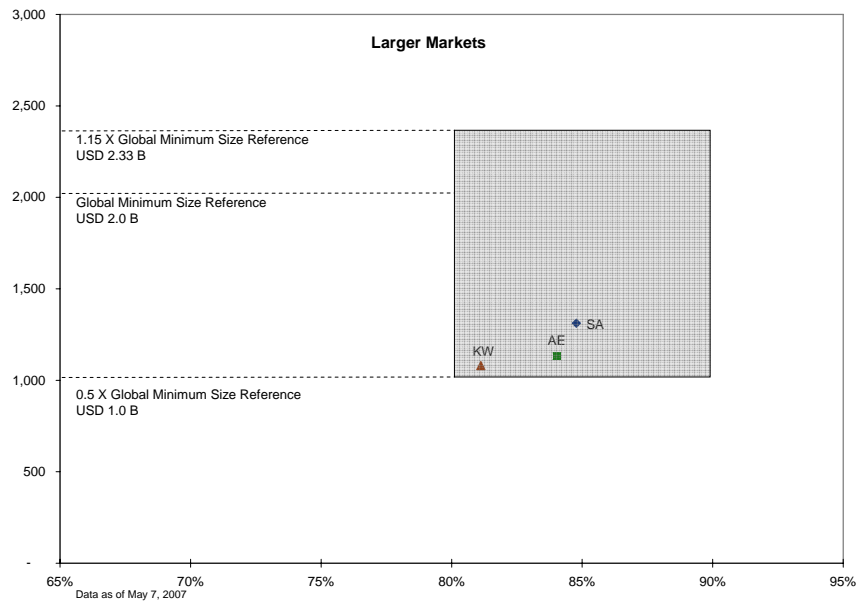
Example: Saudi Arabia

- Companies are counted in descending order of full market capitalization starting with the largest company.
- When the cumulative free float-adjusted market coverage reaches 85%, the full market capitalization of the last company counted is checked to see if it is within the Global Minimum Size Range, which it is in this case.
- The rank of this company in the Saudi Arabia Market Investable Equity Universe is 31 and its market cap is USD 1.3 Billion.
- Thus, the top 31 companies define the large and mid segment in the Saudi Arabia in this example and the cutoff between the mid and the small cap segment is set at Saudi Arabia 1.3 Billion for this market.



Data as of May 7, 2007

Proposed Size and Coverage Target Area for Larger and Smaller Markets



Comparing the current GCC Countries Indices to the Proposed Enhanced GCC Standard Indices

Enhanced GCC Countries Standard Indices

- The number of constituents in the MSCI GCC Countries Index would significantly drop but the free float-adjusted index market capitalization would only be marginally reduced
 - The application of the proposed framework would result in the addition of larger companies and the deletion of smaller companies
- Making no distinction between larger and smaller countries in terms of market size would lead to a sharp decrease in the free float-adjusted index market capitalization for Bahrain, Oman and Qatar

Comparison to the Current GCC Countries Standard Indices (pro forma constituents as of June 1st, 2007)

	Bahrain	Kuwait	Oman	Qatar	Saudi Arabia	United Arab Emirates	GCC Countries
Enhanced GCC Countries Standard Index constituents	3	20	7	8	25	12	75
Current GCC Countries Standard Index constituents	6	46	9	16	31	24	132
Free-Float Adjusted Market Cap of Enhanced GCC Countries Standard Index	1,230	44,897	2,501	8,254	58,718	20,046	135,646
Free-Float Adjusted Market Cap of Current GCC Countries Standard Index	1,659	46,163	2,630	9,821	56,342	20,839	137,454
Market Cap of Deletions	429	6,626	296	1,567	2,382	3,010	14,310
Market Cap of Additions	-	5,360	167	-	4,758	2,217	12,502
Turnover Resulting from Deletions	25.9%	14.4%	11.3%	16.0%	4.2%	14.4%	10.4%
Turnover Resulting from Additions	0.0%	11.9%	6.7%	0.0%	8.1%	11.1%	9.2%
One-way Index Turnover	25.9%	14.4%	11.3%	16.0%	8.1%	14.4%	10.4%

Note: All market caps are in USD millions. Data as of May 7, 2007

Potential Deletions from the Current GCC Country Indices mostly due to move to the Small Cap Indices

- To ensure investability and replicability of size segments, a security's free float-adjusted market capitalization would be required to be at least 50% of the minimum size cut-off for that market
 - Qatar would be the only country impacted by this additional investability requirement
- Only a marginal portion of the total free float-adjusted index market capitalization deleted from the current Standard Indices would not be migrated to the Small Cap Indices

Deleted Free-Float Adjusted Index Market Capitalization and Number of Securities

	Bahrain	Kuwait	Oman	Qatar	Saudi Arabia	United Arab Emirates	GCC Countries
Migration to GCC Countries Small Cap Index	282 2	6,086 28	296 3	981 6	2,382 10	2,878 13	12,905 62
Below Minimum Liquidity Requirement	147 1	541 2	- -	- -	- -	131 1	819 4
Issuer Full Market Cap Above Enhanced Standard Minimum but Security Free-Float Market Cap Below Enhanced Standard Minimum	- -	- -	- -	586 2	- -	- -	586 2
Total Deleted Free-Float Adjusted Index Market Capitalization	282 1	6,086 2	296 -	1,567 2	2,382 -	2,878 1	14,310 68

Note: All market caps are in USD millions. Data as of May 7, 2007

GCC Countries Small Cap Indices

- A large number of GCC Countries Small Cap constituents would result from a migration from the current Standard Indices
 - Kuwait would exhibit the largest number of migrations from the current index to the Small Cap Index
- Saudi Arabia would exhibit the largest number of new additions to the Small Cap Index

GCC Countries Small Cap Index

	Bahrain	Kuwait	Oman	Qatar	Saudi Arabia	United Arab Emirates	GCC Countries
Current GCC Countries Standard Index to GCC Countries Small Cap Index	2	28	3	6	10	13	62
GCC Countries Small Cap Index Constituents	1	28	3	6	32	7	77
Total GCC Countries Small Cap Index Constituents	3	56	6	12	42	20	139
Free-Float Adjusted Market Cap of GCC Small Cap Index	335	10,214	524	1,858	8,993	3,913	25,837

Note: All market caps are in USD millions. Data as of May 7, 2007

GCC Countries Investable Market Indices

- The proposed framework would enable the MSCI GCC Countries Investable Market Index to reach a 94.4% representation of the Investable Universe, based on data as of May 10, 2007
 - Saudi Arabia would be the closest to the Enhanced Standard and Investable Market Index target representations with respectively 84.5% and 97.5%

GCC Countries Investable Market Index

	Bahrain	Kuwait	Oman	Qatar	Saudi Arabia	United Arab Emirates	GCC Countries
Total Enhanced GCC Countries Standard Index Constituents	3	20	7	8	25	12	75
Free-Float Adjusted Market Cap of Enhanced GCC Countries Standard Index	1,230	44,897	2,501	8,254	58,718	20,046	135,646
Enhanced GCC Countries Standard Index as % of Investable Universe	66.3%	81.1%	76.1%	74.9%	84.5%	79.7%	78.9%
Total GCC Countries Small Cap Index Constituents	3	56	6	12	42	20	139
Free-Float Adjusted Market Cap of GCC Small Cap Index	335	10,214	524	1,858	8,993	3,913	25,837
GCC Small Cap Index as % of Investable Universe	18.08%	18.45%	15.95%	16.87%	12.94%	15.56%	15.55%
Total GCC Countries Investable Market Index Constituents	6	76	13	20	67	32	214
Free-Float Adjusted Market Cap of GCC Countries Investable Market Index	1,565	50,274	3,025	10,112	69,459	26,044	161,483
GCC Countries Investable Market Index as % of Investable Universe	84.4%	99.6%	92.0%	91.8%	97.5%	95.3%	94.4%

Note: All market caps are in USD millions. Data as of May 7, 2007

Benefits of the Proposed Framework

- Exhaustive coverage of the investable opportunity set along with non-overlapping size segmentation
- The proposed framework provides a balance between:
 - Consistent investability and replicability requirements
 - vs.
 - Flexibility required to apply this framework to countries of different size and liquidity
- Continuity with the current Standard Index coverage through the targeting of 85% of the investable universe
- Compatibility with the Global Investable Market Indices Methodology



Alternatives

Alternatives

- MSCI Barra could apply a sampling methodology combined with an inclusion rule for large securities
 - Top-down approach to cover the largest securities (top 50% to 70% representation in each market) in terms of free float-adjusted market capitalization
 - Additional (minimum) 85% target representation at Industry Group level
- The transition of the MSCI GCC Countries Indices to the enhanced methodology could take place in two distinct phases

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