

Consultation on Potential Enhancement to MSCI Japan ESG Select Leaders Index Methodology

MARCH 2022

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.

Overview

- MSCI launched a consultation on a proposed change of the parent index for the MSCI Japan ESG Select Leaders Index from MSCI Japan IMI Top 700 Index to MSCI Japan IMI
 - The proposal aims to provide full coverage of the MSCI Japan IMI universe (1,127 securities as of March 22, 2022), following the increased availability of ESG data
- The proposed change would be implemented starting from the May 2022 Semi-Annual Index Review in one of the following ways:
 - **Proposal:** apply the Semi-Annual Index Review rules
 - **Alternative:** apply a full index reconstitution with no priority for existing index constituents

MSCI welcomes feedback from market participants until **April 8, 2022** and will announce its decision on or before **April 15, 2022**

Potential Enhancement

- Change the parent index from MSCI Japan IMI Top 700 to MSCI Japan IMI

Parameters	Methodology
Parent Index (CURRENT)	MSCI Japan IMI Top 700 (ranked by free float market capitalization, 20% buffer)
Parent Index (NEW)	MSCI Japan IMI
ESG Screening (unchanged)	Exclude companies with: <ul style="list-style-type: none"> • ESG Rating below 'BB' (buffer 'B') • ESG Controversy Score below '3' (buffer '1')
ESG Selection (unchanged)	Within each GICS sector, target 50% of the free-float adjusted market capitalization, ranked on certain ESG criteria
Weighting	Each security is weighted by its corresponding free-float adjusted market capitalization

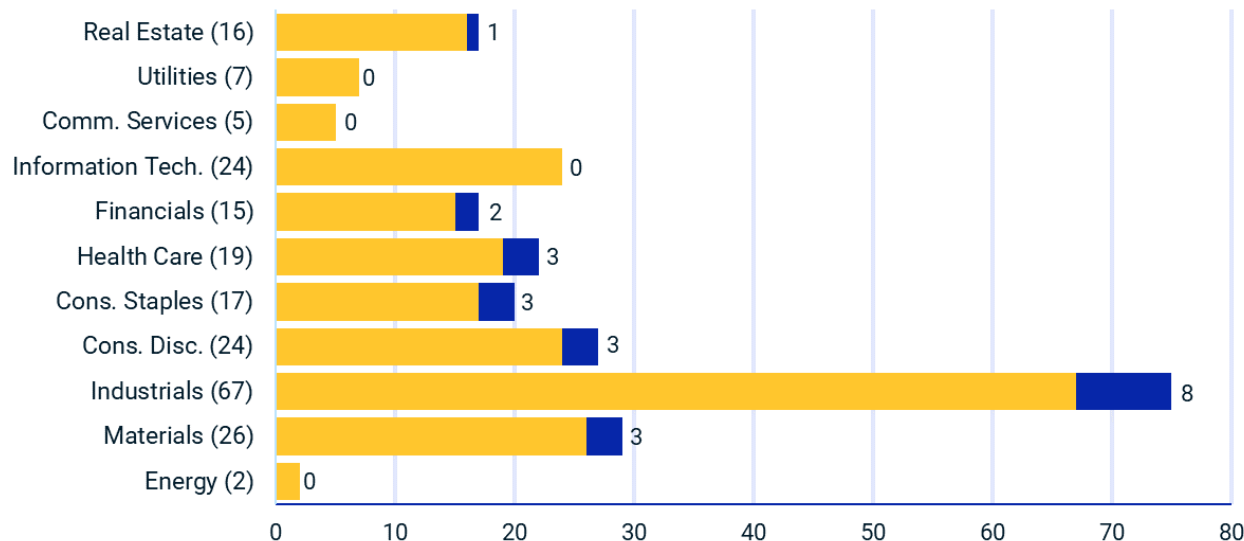


Broader Opportunity Set

Proposal (Semi-Annual Index Review rules):

Changing the parent index would broaden the MSCI Japan ESG Select Leaders Index by 23 securities across 7 of the 11 GICS® sectors

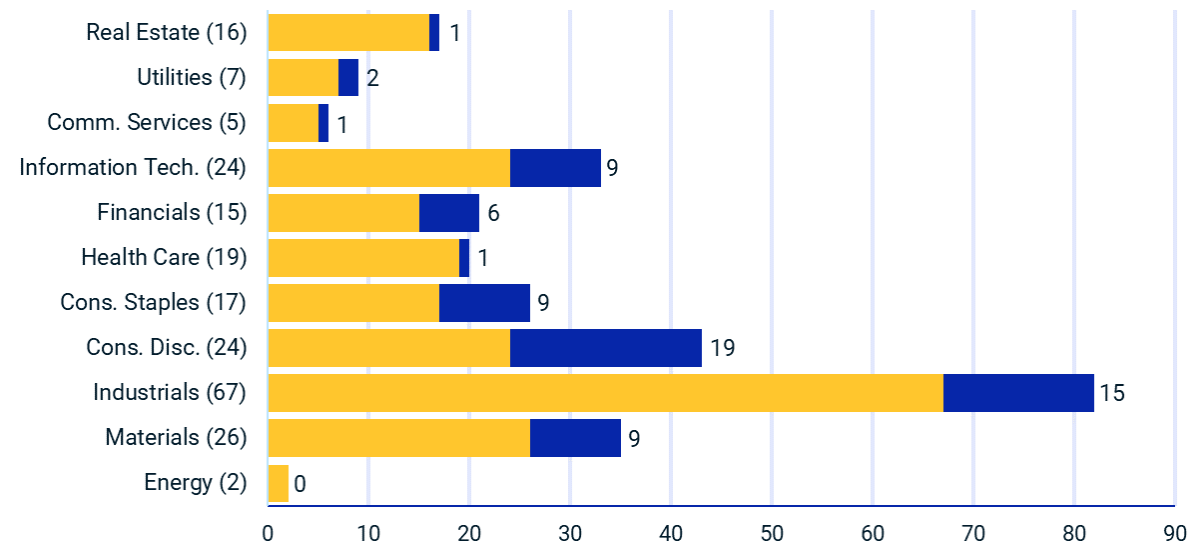
Number of constituents



Alternative (full reconstitution):

Changing the parent index would broaden the MSCI Japan ESG Select Leaders Index by 72 securities across 10 of the 11 GICS® sectors

Number of constituents



Existing Index (Number of Securities)

Additions due to Proposed Universe



Simulations as of the November 2021 Semi-Annual Index Review

Information Classification: GENERAL

Transition Analysis

- Impact of changing the parent index to MSCI Japan IMI if it had been implemented at the November 2021 Semi-Annual Index Review:

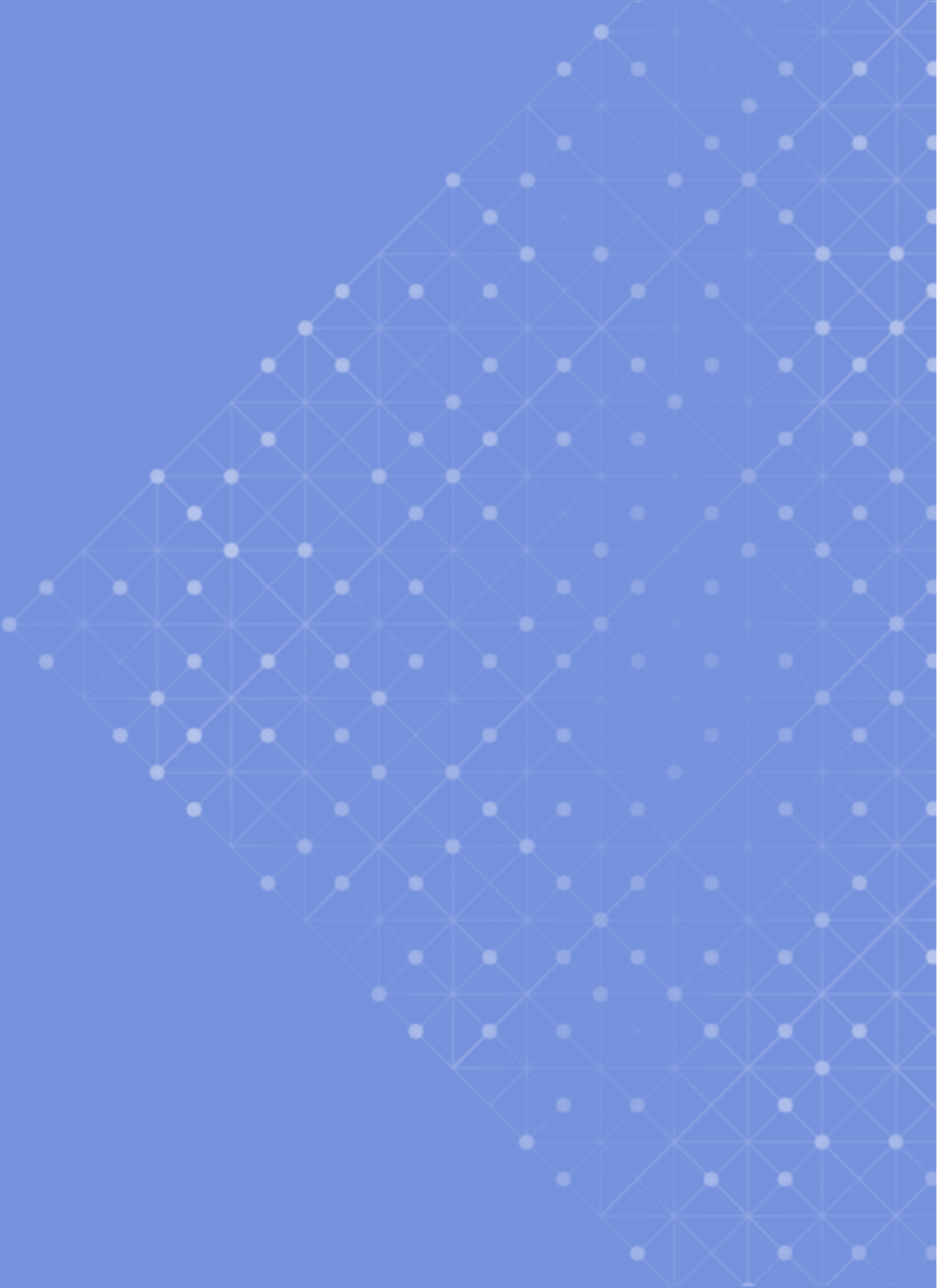
	Additions	Deletion	Turnover
Current	4	10	3.5%
Proposal	23	6	4.6%
Alternative	109	43	16.0%

Simulation as of the November 2021 Semi-Annual Index Review

Discussion Points

- Do you agree with the proposed change of the parent index from the MSCI Japan IMI Top 700 to the MSCI Japan IMI?
- Do you agree to apply the Semi-Annual Index Review rules (including the priority given to existing constituents in the ranking and selection of securities) at the time of the transition?
 - Alternatively, should the Index be fully reconstituted to allow for a better representation of Small Cap companies from the expanded universe, but at the expense of higher turnover at the time of the transition?

Appendix



Ranking and Selection

- Possible ranking and selection options for implementing the proposed change of the parent index from the MSCI Japan IMI Top 700 to the MSCI Japan IMI:

	Proposal: Semi-Annual Index Review rules	Alternative: Full reconstitution
Ranking	<p>For each sector, eligible companies of the Parent Index are ranked based on the following criteria:</p> <ul style="list-style-type: none"> • ESG Ratings • Current index membership (existing constituents above non-constituents) • Industry adjusted ESG scores • Decreasing free float adjusted market capitalization 	<p>For each sector, eligible companies of the Parent Index are ranked based on the following criteria:</p> <ul style="list-style-type: none"> • ESG Ratings • Industry adjusted ESG scores • Decreasing free float adjusted market capitalization
Selection	<p>Constituents for the Index are then selected from the ranked universe in the following order until 50% coverage by cumulative free-float adjusted market capitalization target is reached:</p> <ul style="list-style-type: none"> • Securities in the top 35% • 'AAA' and 'AA' rated securities in the top 50% • Current index constituents in the top 65% • Remaining securities in the eligible universe 	<p>Constituents for the Index are then selected from the ranked universe until 50% coverage by cumulative free-float adjusted market capitalization target is reached.</p>

Detailed Simulated Impact (Proposal)

Proposed implementation: Semi-Annual Index Review rules

GICS Sector	Number of Constituents			Sector Coverage	
	Current*	Additions	Weight of Additions	Current*	Simul.
Energy	2	-	-	65%	64%
Materials	26	3	0.6%	59%	58%
Industrials	67	8	0.2%	50%	50%
Consumer Discretionary	24	3	0.1%	61%	61%
Consumer Staples	17	3	0.2%	49%	49%
Health Care	19	3	0.2%	49%	50%
Financials	15	2	0.5%	48%	49%
Information Technology	24	-	-	58%	58%
Communication Services	5	-	-	55%	56%
Utilities	7	-	-	55%	56%
Real Estate	16	1	0.1%	48%	48%
Total	222	23	1.9%		

Simulation as of the November 2021 Semi-Annual Index Review

* Pro forma constituents of the MSCI Japan ESG Select Leaders Index as of the November 2021 Semi-Annual Index Review

Detailed Simulated Impact (Alternative)

Alternative implementation: full reconstitution

GICS Sector	Number of Constituents					Sector Coverage	
	Current*	Additions	Weight of Additions	Deletions	Weight of Deletions	Current*	Simul.
Energy	2	-	-	-	-	65%	64%
Materials	26	14	1.9%	5	2.6%	59%	50%
Industrials	67	26	2.4%	11	2.2%	50%	50%
Consumer Discretionary	24	21	0.9%	2	1.2%	61%	60%
Consumer Staples	17	9	0.4%	-	-	49%	51%
Health Care	19	3	0.1%	2	0.1%	49%	50%
Financials	15	7	0.6%	1	0.4%	48%	50%
Information Technology	24	13	2.9%	4	5.1%	58%	50%
Communication Services	5	2	0.4%	1	1.4%	55%	48%
Utilities	7	4	0.3%	2	0.3%	55%	51%
Real Estate	16	6	1.1%	5	0.9%	48%	50%
Total	222	105	11.0%	33	14.2%		

Simulation as of the November 2021 Semi-Annual Index Review

* Pro forma constituents of the MSCI Japan ESG Select Leaders Index as of the November 2021 Semi-Annual Index Review

ESG Metrics

Integration, Values and Norms

	MSCI Japan IMI Index	Current	Proposal	Alternative
Integration				
ESG Score	6.2	7.3	7.3	7.5
ESG Leaders (AAA-AA) (%)	30.2	53.4	52.5	53.9
ESG Laggards (B-CCC) (%)	5.8	0	0	0
ESG Trend Positive (%)	31.9	28.9	29.3	34.5
ESG Trend Negative (%)	4.4	4.1	4.2	3.9
Index ESG Rating	AA	AAA	AAA	AAA
Environmental Pillar Score	5.7	6.2	6.2	6.2
Social Pillar Score	5.4	5.9	5.9	5.9
Governance Pillar Score	4.7	4.8	4.8	5
Key Governance Metrics				
Board Independence (wtd Avg %)	44.1	43.6	43.6	43.8
Female Directors (wtd Avg %)	13.9	14.9	14.9	15.2
Deviation from One Share One Vote (%)	6.2	10.4	10.2	9.2
Values and Norms				
Tobacco Involvement (%)	1.4	0.1	0.1	0.1
Civilian Firearms Producers (%)	0.1	0.1	0.1	0.1
Ties to Controversial Weapons (%)	0	0	0	0
Global Compact Compliance Violation (%)	0.1	0	0	0
Red Flag Controversies (%)	0.1	0	0	0
Orange Flag Controversies (%)	5.9	0.9	0.9	0

As of February 28, 2022.

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Contact Us

AMERICAS	EUROPE, MIDDLE EAST & AFRICA	ASIA PACIFIC
Americas +1 888 588 4567 *	Cape Town + 27 21 673 0100	China North 10800 852 1032 *
Atlanta + 1 404 551 3212	Frankfurt + 49 69 133 859 00	China South 10800 152 1032 *
Boston + 1 617 532 0920	Geneva + 41 22 817 9777	Hong Kong + 852 2844 9333
Chicago + 1 312 675 0545	London + 44 20 7618 2222	Mumbai + 91 22 6784 9160
Monterrey + 52 81 1253 4020	Milan + 39 02 5849 0415	Seoul 00798 8521 3392 *
New York + 1 212 804 3901	Paris 0800 91 59 17 *	Singapore 800 852 3749 *
San Francisco + 1 415 836 8800		Sydney + 61 2 9033 9333
São Paulo + 55 11 3706 1360		Taipei 008 0112 7513 *
Toronto + 1 416 628 1007		Thailand 0018 0015 6207 7181 *
* = toll free		Tokyo +81 3 5290 1555
msci.com		
clientservice@msci.com		
esgclientservice@msci.com		

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