

# Consultation on the MSCI Corporate Bond Indexes Methodology

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## INDEX METHODOLOGY CHANGE PROPOSAL

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 result of the consultation.

**November 2023**

# Executive Summary

- The MSCI Corporate Bond Indexes are constructed to measure the performance of eligible corporate bonds issued in certain credit markets.
- MSCI proposes the following updates to the existing methodology to further enhance the replicability of the MSCI Corporate Bond Indexes :
  - *Introducing a liquidity screen based on the MarketAxess Relative Liquidity Score data to exclude illiquid bonds from the indexes.*
  - *Implementing an issuer ticker cap to guard against issuer concentration risk in the MSCI Corporate Bond Indexes.*
  - *Introducing a 12-month lock-out period for index deletions to reduce reverse turnover in the indexes.*
- MSCI welcomes feedback from market participants until **January 15, 2024**, and will announce the results of the consultation by **end of January 2024**.

# Methodology Proposal – MSCI Corporate Bond Indexes

Inclusion criteria	Current Methodology	Proposed Methodology Changes
<b>Issuer Country of Domicile</b>	Developed Markets	Developed Markets
<b>Issuer type</b>	Corporate debt only	Corporate debt only
<b>Min time to maturity</b>	1 year for current bond constituents, 1.5 years for new entrants	1 year for current bond constituents, 1.5 years for new entrants
<b>Size screen</b>	USD Core IG – 750m, USD HY – 200m EUR IG – 300m, USD HY – 150m GBP IG – 200m, GBP HY – 100m	USD Core IG – 750m, USD HY – 200m EUR IG – 300m, USD HY – 150m GBP IG – 200m, GBP HY – 100m
<b>Lock out period</b>	-	<b>12 months</b>
<b>Liquidity Screen</b>	-	<b>Liquidity Score* &gt; 1</b> <i>No Liquidity Screen for the MSCI CAD Corporate Bond Indexes.</i>
<b>Security Weighting</b>	Market Cap Weighted	Market Cap Weighted with Issuer cap
<b>Issuer Capping</b>	-	<b>Capping of 3%</b> <i>(5% for MSCI CAD IG Corporate Bond Index; No Capping for the MSCI GBP HY &amp; CAD HY Corporate Bond Indexes)</i>
<b>Rating</b>	Min Moody's / S&P rating: Baa3 / BBB-	Min Moody's / S&P rating: Baa3 / BBB-
<b>Rebalancing</b>	Monthly	Monthly
<b>Pricing source</b>	Refinitiv as primary source and ICE as secondary	Refinitiv as primary source and ICE as secondary



\*Simple average of MarketAxess Relative Liquidity Score calculated over a 21-day rolling window.

# Simulated impact of including the liquidity screen (1/2)

Index Name	USD IG Core	USD HY	EUR IG	EUR HY	GBP IG	GBP HY
<b>Number of Constituents</b>						
Current	3760	2029	3310	568	819	81
Alternative 1 – Exclude Liquidity Score = 0	3743 (-0.5%)	2006 (1.1%)	3241 (-2.1%)	565 (-0.5%)	810 (-1.1%)	80 (1.2%)
Alternative 2 – Exclude Liquidity Score <= 1	<b>3740 (-0.5%)</b>	<b>1921 (-5.3%)</b>	<b>3188 (-3.7%)</b>	<b>554 (-2.5%)</b>	<b>803 (-2.0%)</b>	<b>78 (-3.7%)</b>
Alternative 3 – Exclude Liquidity Score <= 2	3718 (-1.1%)	1723 (-15.1%)	3073 (-7.2%)	532 (-6.3%)	795 (-2.9%)	71 (-12.3%)
<b>Market Value Coverage (%)</b>						
Current	100.0	100.0	100.0	100.0	100.0	100.0
Alternative 1 – Exclude Liquidity Score = 0	99.7 (-0.3%)	99.3 (-0.7%)	98.4 (-1.6%)	99.8 (-0.2%)	98.8 (-1.2%)	98.9 (-1.1%)
Alternative 2 – Exclude Liquidity Score <= 1	<b>99.6 (-0.4%)</b>	<b>97.4 (-2.6%)</b>	<b>97.5 (-2.5%)</b>	<b>98.9 (-1.1%)</b>	<b>98.3 (-1.7%)</b>	<b>97.7 (-2.3%)</b>
Alternative 3 – Exclude Liquidity Score <= 2	99.3 (-0.7%)	92.5 (-7.5%)	95.5 (-4.5%)	97.0 (-3.0%)	97.8 (-2.2%)	93.1 (-6.9%)
<b>Average RLS Score</b>						
Current	6.93	5.31	6.73	6.03	6.76	5.97
Alternative 1 – Exclude Liquidity Score = 0	7.48 (8%)	6.46 (22%)	7.39 (10%)	6.70 (11%)	7.40 (9%)	6.75 (13%)
Alternative 2 – Exclude Liquidity Score <= 1	<b>7.49 (8%)</b>	<b>6.56 (24%)</b>	<b>7.45 (11%)</b>	<b>6.75 (12%)</b>	<b>7.43 (10%)</b>	<b>6.82 (14%)</b>
Alternative 3 – Exclude Liquidity Score <= 2	7.50 (8%)	6.83 (29%)	7.57 (12%)	6.85 (14%)	7.46 (10%)	7.08 (19%)

# Simulated impact of including the liquidity screen (2/2)

Index Name	USD IG Core	USD HY	EUR IG	EUR HY	GBP IG	GBP HY
<b>Number of Issuer Tickers</b>						
Current	495	916	603	286	275	51
Alternative 1 – Exclude Liquidity Score = 0	494 (-0.2%)	902 (-1.5%)	603	285 (-0.3%)	274 (-0.4%)	50 (-2.0%)
<b>Alternative 2 – Exclude Liquidity Score &lt;= 1</b>	<b>493 (-0.4%)</b>	<b>845 (-7.8%)</b>	<b>597 (-1.0%)</b>	<b>277 (-3.1%)</b>	<b>269 (-2.2%)</b>	<b>48 (-5.9%)</b>
Alternative 3 – Exclude Liquidity Score <= 2	486 (-1.8%)	740 (-19.2%)	579 (-4.0%)	265 (-7.3%)	265 (-3.6%)	43 (-15.7%)
<b>Maximum Ticker Weight (%)</b>						
Current	3.52	5.08	2.59	3.11	1.97	9.25
Alternative 1 – Exclude Liquidity Score = 0	3.54 (0.6%)	5.12 (0.8%)	1.83 (-29.3%)	3.12 (0.3%)	1.95 (-1.0%)	9.36 (1.2%)
<b>Alternative 2 – Exclude Liquidity Score &lt;= 1</b>	<b>3.54 (0.6%)</b>	<b>5.22 (2.8%)</b>	<b>1.85 (-28.6%)</b>	<b>3.15 (1.3%)</b>	<b>1.96 (-0.5%)</b>	<b>9.47 (2.4%)</b>
Alternative 3 – Exclude Liquidity Score <= 2	3.55 (0.9%)	5.50 (8.3%)	1.87 (-27.8%)	3.21 (3.2%)	1.97	9.94 (7.5%)
<b>Proposed Issuer Ticker Weight Cap (%)</b>	<b>3</b>	<b>3</b>	<b>3</b>	<b>3</b>	<b>3</b>	<b>-</b>

# Simulated Impact of including the issuer ticker cap - Top 5 Issuer Tickers by Weight (1/2)

Maximum Ticker Weight (%)	USD IG Core	USD HY
Maximum Issuer Ticker Weight	3.54	5.22
# of Issuer Tickers	493	845
Proposed Issuer Weight Cap (%)	3	3

## USD IG Core

## USD HY

Issuer Ticker	Issuer Name	Current	Proposal
BAC	Bank of America	3.54	3.00 (-15.3%)
JPM	JPMorgan Chase & Co	3.10	3.00 (-3.2%)
MS	Morgan Stanley	2.46	2.47 (0.4%)
WFC	Wells Fargo & Co	2.26	2.27 (0.4%)
C	Citi Group Inc	2.02	2.04 (1.0%)

Issuer Ticker	Issuer Name	Current	Proposal
CHTR	Charter Communications Operating LLC	5.22	3.00 (-42.5%)
F	Ford Motor Company	3.02	3.00 (-0.7%)
OXY	Occidental Petroleum Corp	1.14	1.17 (2.6%)
CNC	Centene Corp	1.07	1.09 (1.9%)
TDG	Transdigm Inc	1.00	1.02 (2.0%)

# Simulated Impact of including the issuer ticker cap - Top 5 Issuer Tickers by Weight (2/2)

Maximum Ticker Weight (%)	EUR IG	EUR HY	GBP IG	GBP HY	CAD IG	CAD HY
Maximum Issuer Ticker Weight	1.85	3.15	1.96	9.47	9.18	11.04
# of Issuer Tickers	597	277	269	48	117	29
Proposed Issuer Weight Cap (%)	3	3	3	-	5	-

*No Capping for the MSCI CAD HY Corporate Bond Index and MSCI GBP HY Corporate Bond Index due to the concentrated nature of the universe.*

## EUR HY

Issuer Ticker	Issuer Name	Current	Proposal
TLIT	Telecom Italia SPA	3.15	3.00 (-4.8%)
CLNX	Cellnex Telecom SA	2.66	2.67 (0.4%)
TEVA	TEVA Pharmaceutical Finance Netherlands	2.18	2.19 (0.5%)
BAMI	Banco BPM SPA	2.07	2.07
FRVIA	Forvia SE	1.89	1.89

## CAD IG

Issuer Ticker	Issuer Name	Current	Proposal
TD	Toronto Dominion Bank	9.18	5.00 (-45.5%)
RY	Royal Bank of Canada	8.22	5.00 (-39.2%)
ENB	Enbridge Inc	7.24	5.00 (-30.9%)
BMO	Bank of Montreal	6.40	5.00 (-21.9%)
BCE	Bell Telephone Company of Canada	4.77	5.00 (4.8%)



Data as of September 1<sup>st</sup>, 2023.

# Simulated Turnover Impact of including a Lock-Out Period

On average, including a 12-month lock-out period lowers the turnover across indexes

Index	USD IG Core			EUR IG			GBP IG			
	Rebalancing Turnover	Pre-Lock-Out	Post-Lock-Out	Lock-out Impact	Pre-Lock-Out	Post-Lock-Out	Lock-out Impact	Pre-Lock-Out	Post-Lock-Out	Lock-out Impact
February 2023		2.24%	2.20%	<b>-0.04%</b>	3.09%	2.83%	<b>-0.26%</b>	2.49%	2.49%	<b>0.00%</b>
March 2023		1.79%	1.68%	<b>-0.10%</b>	1.83%	1.60%	<b>-0.24%</b>	3.02%	3.01%	<b>-0.01%</b>
April 2023		2.60%	2.50%	<b>-0.10%</b>	2.55%	2.07%	<b>-0.48%</b>	3.26%	1.32%	<b>-1.94%</b>
May 2023		1.26%	1.18%	<b>-0.08%</b>	1.84%	1.55%	<b>-0.29%</b>	1.15%	0.96%	<b>-0.19%</b>
June 2023		3.43%	3.36%	<b>-0.07%</b>	3.20%	3.05%	<b>-0.15%</b>	1.93%	1.91%	<b>-0.02%</b>
July 2023		2.23%	2.00%	<b>-0.23%</b>	2.57%	2.35%	<b>-0.22%</b>	2.14%	2.19%	<b>0.05%</b>
August 2023		1.41%	1.38%	<b>-0.04%</b>	1.59%	1.49%	<b>-0.10%</b>	1.15%	1.15%	<b>0.01%</b>
September 2023		1.73%	1.61%	<b>-0.12%</b>	0.97%	0.54%	<b>-0.43%</b>	1.25%	1.24%	<b>-0.01%</b>
October 2023		1.57%	1.55%	<b>-0.02%</b>	2.64%	2.13%	<b>-0.50%</b>	1.74%	1.75%	<b>0.01%</b>
<b>Average Turnover Impact of including Lockout</b>				<b>-0.09%</b>			<b>-0.30%</b>			<b>-0.23%</b>



# Consultation Questions

## Liquidity Screen

- With a view to balance liquidity and representativeness of the index, the proposal is to only screen out bonds that have a liquidity score of less than or equal to one:
  - Do you agree with the proposed liquidity screen? If not, then do you prefer Alternative 1 or Alternative 3?

## Issuer Capping

- Do you agree with the implementation of a new methodology rule to include a 3% issuer ticker cap in the GBP IG, USD & EUR Corporate Bond Indexes?
- Do you agree with the implementation of 5% issuer ticker cap in the MSCI CAD IG Corporate Bond Index Methodology?
- Do you agree with not applying capping on MSCI GBP HY Corporate Bond Index and MSCI CAD HY Corporate Bond Index?

## Lock-Out Period

- Do you agree with the addition of a 12-month lock out period for index deletions to control for reverse turnover?

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