

INDEX INSIGHTS



A look into the May 2023 MSCI Quarterly Comprehensive Index Review

By iShares Global Research & Analytics and Product Consulting

It's important for investors to monitor index rebalances. Updates to index holdings, like additions, deletions, and weight changes, may have a corresponding impact on iShares ETFs.¹ In this edition of *Index Insights*, we explore what we expect to happen during the May 2023 MSCI Quarterly Comprehensive Index Review, including:

- **Finalizing changes to the quarterly index review process.** The MSCI Global Investable Market Indexes (GIMI) transitioned to a quarterly comprehensive index review (QCIR) schedule as part of the February 2023 index review.² However, changes to number of shares (NOS) and foreign inclusion factor (FIF) review criteria will be implemented at the May 2023 QCIR.
- **Heightened turnover in MSCI flagship market capitalization and Factor Indexes.**³ Turnover is expected to increase in certain developed and emerging market MSCI Indexes, especially small cap indexes. Separately, certain MSCI Factor Indexes are expected to have notable additions and deletions which are expected to have significant impact on turnover levels.
- **MSCI announced additional Chinese securities are expected to be added to the MSCI Emerging Markets Index as a result of March 2023 Northbound Stock Connect universe expansion.**⁴ Changes to the program are expected to make an additional 51 companies eligible for inclusion in the MSCI Emerging Markets Index, which is expected to increase China's weight in the index following the May QCIR.

Featured iShares ETFs

SCZ	iShares MSCI EAFE Small-Cap ETF	EEMS	iShares MSCI Emerging Markets Small-Cap ETF	QUAL	iShares MSCI USA Quality Factor ETF
IEFA	iShares Core MSCI EAFE ETF	IEMG	iShares Core MSCI Emerging Markets ETF	EEM	iShares MSCI Emerging Markets ETF
ACWI	iShares MSCI ACWI ETF	MTUM	iShares MSCI USA Momentum Factor ETF		

Moving ahead with the MSCI Quarterly Comprehensive Index Reviews

As part of the recent changes to MSCI's Index review process, there were numerous updates, including moving to four uniform quarterly comprehensive index reviews. However, a few additional changes were staggered and are expected to be implemented as part of the May 2023 MSCI QCIR, including:

- **Changes to number of shares review criteria.**⁵ Changes in shares outstanding can occur for numerous reasons including if a company buys back stock (which reduces the number of shares outstanding) or corporate actions such as a spin-off (which impacts the number of shares outstanding). By changing the criteria of reviews, NOS will be adjusted for each security on a more frequent basis.
- **Updating the foreign inclusion factor criteria.**⁶ FIFs represent how much of a company's free-float is available to international investors.⁷ It provides a more accurate gauge of investability of foreign securities for U.S. investors. As a result, the FIF adjusts the weight of each security within MSCI global equity indexes. Changes to the FIF review process as part of the May 2023 QCIR will result in more frequent FIF calculations.

As a result of these final changes, overall index turnover levels may increase at the May 2023 QCIR compared to the inaugural February 2023 QCIR. However, QCIR turnover levels may be lower than during the previous semi-annual index reviews going forward.

Notable one-way turnover of MSCI Indexes

Index turnover measures the percentage change in the composition of an index over a specific period.⁸ Additions to or deletions from an index can be a major driver of index turnover during a rebalance. It's important for BlackRock's index fund managers to monitor turnover levels, as they can dictate the amount of trading activity that may need to take place in a particular fund during a rebalance.

Certain broad-based MSCI Indexes that iShares ETFs seek to track may have elevated one-way turnover for the May QCIR. **Notably, turnover may increase in small cap indexes, particularly within emerging markets** (the implementation of the additional QCIR criteria may be a contributor) (**Figure 1**).

There are also certain MSCI Factor Indexes that are expected to see high levels of turnover. Factor or "active risk" indexes seek to capture "alternative" risk considerations (via market timing or security selection) by assessing other stock-level characteristics, such as style factors (quality, value, size, momentum, volatility) or dividend yields.⁹ Active risk benchmarks utilize methodology which deviates from traditional market-capitalization weighting, and therefore, take active risk relative to market-capitalization weighted indexes. Because of their unique strategies, these indexes typically exhibit higher turnover than market cap-weighted indexes.

- The MSCI USA Momentum SR index, which the **iShares MSCI USA Momentum Factor ETF (MTUM)** seeks to track, is expected to see its one-way turnover increase by nearly 25% versus the November 2022 Semi-Annual Index Review. The expected turnover is a result of a few large additions from the Information Technology sector (Microsoft and Nvidia) and Meta Platforms Inc. (Communication Services) with deletions of UnitedHealth Group (Health Care) and Chevron Corp (Energy).¹⁰
- The MSCI USA Sector Neutral Quality Gross Index, which the **iShares MSCI USA Quality Factor ETF (QUAL)** seeks to track, is expected to have an approximately 26% one-way turnover in line with the November 2022 Semi-Annual Index Review. The expected turnover is a result of a few additions including ConocoPhillips (Energy) and PepsiCo Inc. (Consumer Staples) and the deletion of Home Depot (Consumer Discretionary).¹¹

Figure 1: Notable expected one-way index turnover for MSCI May 2023 QCIR (%)¹²

MSCI Index	Adds	Deletes	May 2023 QCIR expected one-way turnover (%)	February 2023 QCIR one-way turnover (%)	Change in one-way turnover (%)	Impacted iShares ETFs
MSCI EAFE Small Cap Index [®]	45	35	3.08	1.34	1.74	iShares MSCI EAFE Small-Cap ETF (SCZ)
MSCI Emerging Markets Small Cap Index	94	41	5.81	3.04	2.77	iShares MSCI Emerging Markets Small-Cap ETF (EEMS)
MSCI EAFE IMI Index [®]	43	29	1.00	0.27	0.74	iShares Core MSCI EAFE ETF (IEFA)
MSCI Emerging Markets IMI Index	150	53	2.55	0.56	1.99	iShares Core MSCI Emerging Markets ETF (IEMG)
MSCI ACWI Index	86	37	0.88	0.43	0.45	iShares MSCI ACWI ETF (ACWI)

Table Description: Table showing the expected one-way turnover of certain MSCI Indexes using pro-forma index data provided by MSCI. Pro-forma index data is the projected new index composition following the May 2023 MSCI Quarterly Comprehensive Index Review, which is effective after market close on May 31, 2023.

MSCI ACWI Index sector changes

With roughly 2,880 constituent securities across 23 developed and 24 emerging markets, the MSCI ACWI Index is often used as a barometer for the state of global equity markets.¹³ Changes in expected sector weights in the MSCI ACWI Index during a rebalance period can provide useful insights into how various sectors have performed since the last index review in February 2023 (**Figure 2**). May 2023's QCIR is expected to include a few notable sector shifts as a result of the recent Global Industry Classification Standard (GICS®) changes which took place in March 2023, but are expected to be implemented as part of the May QCIR.¹⁴

- **Increased expected weight to Financials and a down weight to Information Technology.** This is driven by expected migrations of Visa Inc, Mastercard Inc, and PayPal Holdings Inc. from the Information Technology sector to the Financials Sector.¹⁵

Figure 2: May 2023 expected MSCI ACWI Index sector changes (%)¹⁶

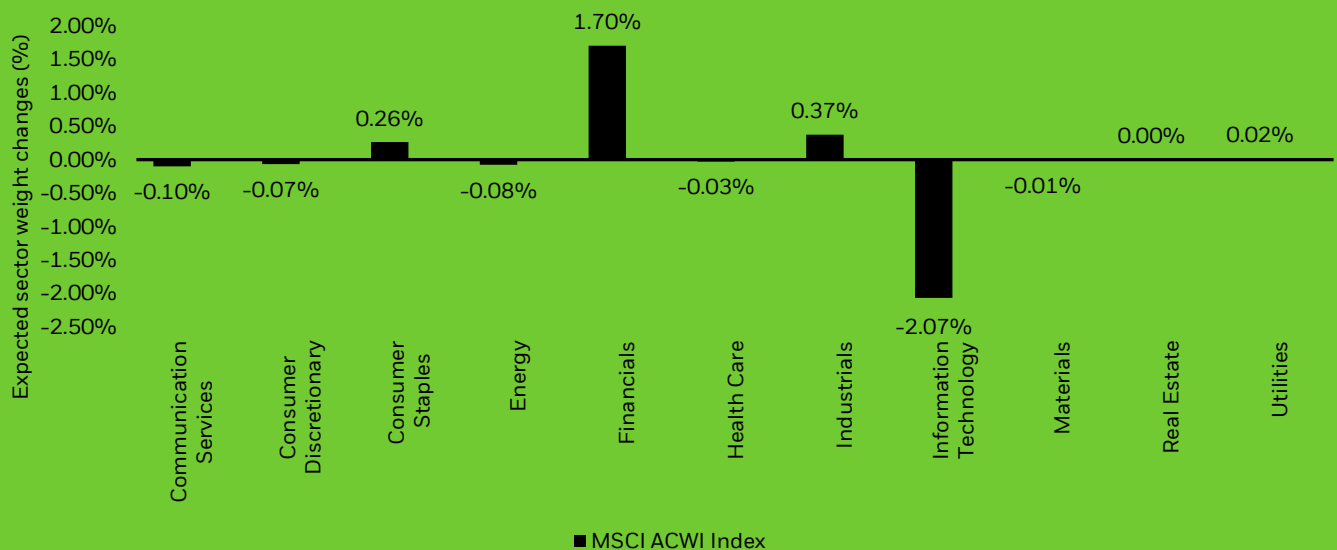


Table Description: Table showing the expected changes in sector weights of the MSCI ACWI Index using pro-forma index data provided by MSCI. Pro-forma index data is the projected new index composition following the May 2023 MSCI Quarterly Comprehensive Index Review, which is effective after market close on May 31, 2023.

An expected increase in Chinese securities within the MSCI Emerging Markets Index

Earlier this year, Hong Kong Exchanges and Clearing Limited (HKEX) announced the expansion of eligible stocks under the Stock Connect program, which took effect on March 13, 2023.¹⁷ This further expanded eligibility of both Northbound and Southbound trading. Northbound trading eligibility refers to the ability for foreign investors to invest in mainland China A-Shares through brokers in Hong Kong. Southbound trading eligibility refers to shares of international companies that have primary listings in Hong Kong and can be traded by mainland Chinese investors.

For the May 2023 MSCI QCIR, **MSCI announced** that as a result of the Stock Connect Northbound universe expansion, 51 China A-share securities are expected to be included in the MSCI Emerging Markets Index. In total, there will be 53 additions of Chinese securities to the MSCI Emerging Markets Index, while 12 Chinese securities will be deleted from the index. We expect that these changes, coupled with other standard rebalance activity, will result in China's weight in the MSCI Emerging Markets Index increasing by 0.35% to roughly 30.94%.¹⁸ The **iShares MSCI Emerging Markets ETF (EEM)** seeks to track the MSCI Emerging Markets Index.

Endnotes

1. For more information on managing equity index rebalances, see “[iShares Investigates: Market Indexes and Index Investing: Equity index rebalances.](#)”
2. Changes are effective after the close on May 31. For more information on the MSCI Index review changes, see https://www.msci.com/documents/1296102/33887102/Index+Rebalancing+Brochure+2023.pdf?utm_medium=social&utm_term=Indexes&utm_content=100003801214071
3. Pre-rebalance index data as of market open on May 19, 2023 and expected post-rebalance index data is an estimate of expected values as of market close on May 31, 2023. Source: MSCI.
4. Mainland China and Hong Kong regulators created a cross-border stock trading link, by launching the Shanghai Connect in 2014 and Shenzhen Connect two years later. Stock Connect allows foreign investors to invest in China A-Shares through brokers in Hong Kong (northbound trading) and mainland Chinese investors to invest in Hong Kong stocks through brokers in China (southbound trading). For more information, see https://www.hkex.com.hk/-/media/HKEX-Market/Mutual-Market/Stock-Connect/Getting-Started/Information-Booklet-and-FAQ/Information-Book-for-Investors/Investor_Book_En.pdf
5. A company’s shares outstanding (or outstanding shares) are the total number of shares issued and actively held by stockholders—both outside investors and corporate insiders. Changes in shares outstanding can occur if a company buys back stock (which reduces the number of shares outstanding) or splits its stock (which increases the number of shares outstanding). A decrease in shares outstanding for a company can reduce the weight of that company within an index. Changes in number of shares (NOS) outstanding may be also be impacted by events such as corporate actions, like a spin-off, which may increase or reduce shares outstanding for a particular security. For more information on MSCI’s Index methodologies, see https://www.msci.com/eqb/methodology/meth_docs/MSCI_GIMIMethodology_May2023.pdf
6. The foreign inclusion factor (FIF) of a security is defined as the proportion of shares outstanding that is available for purchase in the public equity markets by international investors. This proportion accounts for the available free float of and/or the foreign ownership limits applicable to a specific security. For more information on MSCI’s Index methodologies, see https://www.msci.com/eqb/methodology/meth_docs/MSCI_GIMIMethodology_May2023.pdf
7. The free-float market cap is the total value of all shares of a stock that are currently available in the market. That excludes shares allocated with exercise rights to executives and other interested parties. An increase in float means that more of a company’s shares can be traded in the market and thus more investable which can increase the weight of a company. For more information on MSCI’s Index methodologies, see https://www.msci.com/eqb/methodology/meth_docs/MSCI_GIMIMethodology_May2023.pdf
8. Index turnover is a measure of weight changes to an index resulting from the rebalancing of the index. One-way turnover views turnover from the perspective of either buying or selling securities in an index. Two-way turnover reflects both the buying and selling of securities in an index.
9. For more information on factor investing, see <https://www.ishares.com/us/strategies/smart-beta-investing>
10. Pre-rebalance index data as of market open on May 19, 2023 and expected post-rebalance index data is an estimate of expected values as of market close on May 31, 2023. Source: BlackRock, MSCI.
11. Pre-rebalance index data as of market open on May 19, 2023 and expected post-rebalance index data is an estimate of expected values as of market close on May 31, 2023. Source: BlackRock, MSCI.
12. Pre-rebalance index data as of market open on May 16, 2023 and expected post-rebalance index data is an estimate of expected values as of market close on May 31, 2023. Source: BlackRock, MSCI.
13. For more information on the MSCI ACWI Index, see: <https://www.msci.com/our-solutions/indexes/acwi>
14. For more information on the recent Global Industry Classification Standard (GICS®) changes, see https://www.spglobal.com/spdji/en/documents/indexnews/announcements/20220331-1451156/1451156_gicsstructurechangedoc31march2022.pdf
15. Pre-rebalance index data as of market open on May 17, 2023 and expected post-rebalance index data is an estimate of expected values as of market close on May 31, 2023. Source: BlackRock, MSCI.
16. Pre-rebalance index data as of market open on May 17, 2023 and expected post-rebalance index data is an estimate of expected values as of market close on May 31, 2023. Source: BlackRock, MSCI.
17. For more information on the expansion of Stock Connect program eligibility, see https://www.hkex.com.hk/News/News-Release/2023/230303news?sc_lang=en
18. Pre-rebalance index data as of market close on May 19, 2023 and expected post-rebalance index data is an estimate of expected values as of market close on May 31, 2023. Source: BlackRock, MSCI.

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