



IHS Markit™

# IHS Markit Consultation on the ESG Methodology update for 3 iBoxx MSCI ESG Liquid Investment Grade Ultrashort Indices

## 1. IHS Markit's Administration

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IHS Markit Benchmark Administration Limited (**IMBA UK**) is the Index Administrator of the iBoxx indices. IMBA UK administers the indices in accordance with the International Organisation of Securities Commissions Principles for Financial Benchmarks (the IOSCO Principles) and the UK Benchmarks Regulation (UK BMR).

## 2. Background

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IMBA UK administers more than 33,000 benchmarks across asset classes, including fixed income, derivatives, economic indicators, equity and commodities, and both proprietary and third-party benchmarks.

The iBoxx MSCI ESG EUR Liquid Investment Grade Ultrashort Index, the iBoxx MSCI ESG GBP Liquid Investment Grade Ultrashort Index, and the iBoxx MSCI ESG USD Liquid Investment Grade Ultrashort Index screen out issuers from the respective iBoxx Liquid Investment Grade Ultrashort reference index (iBoxx EUR Liquid Investment Grade Ultrashort Index / iBoxx GBP Liquid Investment Grade Ultrashort Index / iBoxx USD Liquid Investment Grade Ultrashort Index) that are involved in business lines or activities, as captured by MSCI ESG Research data, such as weapons, firearms, tobacco, adult entertainment, alcohol, gambling, nuclear power, genetically modified organisms, fossil fuel extractives, power generated by the use of fossil fuels, and violators of global norms, specifically the UNGC. Additionally, issuers scoring below a defined threshold based on MSCI ESG Ratings are excluded, as well as those with a notable controversy related to their operations and/or products with a very severe social or environmental impact. Further information about the MSCI ESG research screening can be found on the documentation website under 'Rules Liquid' [here](#).

The indices are an integral part of the global Markit iBoxx index families, which provide the marketplace with accurate and objective indices by which to assess the performance of bond markets and investments.

| Index Name  | ISIN (TRi)   | Ticker (TRi) | RIC (TRi) |
|---|--------------|--------------|-----------|
| iBoxx MSCI ESG EUR Liquid Investment Grade Ultrashort Index | GB00BKYPJT25 | IBXXEUES     | .IBXXEUES |
| iBoxx MSCI ESG GBP Liquid Investment Grade Ultrashort Index | GB00BKYPJF88 | IBXXGES1     | .IBXXGES1 |
| iBoxx MSCI ESG USD Liquid Investment Grade Ultrashort Index | GB00BKYPKB14 | IBXXUES1     | .IBXXUES1 |

## 3. Proposal

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IMBA UK proposes to update the ESG methodology of the 3 iBoxx MSCI ESG Liquid Investment Grade Ultrashort indices to enhance the Climate Change Metrics methodology and other Business Involvement Screenings. Proposed changes to the indices are:

- Update the **MSCI ESG Business Involvement Screening** methodology (exclusion driven by exposure to the following activities), mainly from an absolute revenue threshold to a percentage revenue threshold:
  - Adult Entertainment
    - All companies deriving 5% or more revenue from production of adult entertainment materials are excluded
    - All companies deriving 15% or more revenue from the production, distribution and retail of adult entertainment materials are excluded
  - Alcohol
    - All companies deriving 5% or more revenue from the production of alcohol-related products are excluded
    - All companies deriving 15% or more revenue from the production, distribution, retail and supply of alcohol-related products are excluded
  - Gambling
    - All companies deriving 5% or more revenue from ownership or operation of gambling facilities are excluded
    - All companies deriving 15% or more revenue from gambling-related business activities are excluded
  - Nuclear Weapons
    - All issuers classified as involved in manufacturing of nuclear weapons, nuclear weapons components, manufacturing or assembly of nuclear weapons delivery platforms, or components of nuclear-exclusive delivery platforms are excluded. More specifically:
      - All companies that manufacture nuclear warheads and/or whole nuclear missiles are excluded
      - All companies that manufacture components for nuclear-exclusive delivery platforms are excluded

- All companies that provide auxiliary services related to nuclear weapons are excluded
- All companies that manufacture components that were developed or are significantly modified for exclusive use in nuclear weapons are excluded
- All companies that manufacture components that were not developed or not significantly modified for exclusive use in nuclear weapons but can be used in nuclear weapons are excluded
- All companies that manufacture or assemble delivery platforms that were developed or significantly modified for the exclusive delivery of nuclear weapons are excluded
- All companies that manufacture or assemble delivery platforms that were not developed or not significantly modified for the exclusive delivery of nuclear weapons but have the capability to deliver nuclear weapons are excluded
- Weapons
  - All companies deriving 5% or more revenue from the production of conventional weapons and components are excluded
  - All companies deriving 15% or more aggregate revenue from weapons systems, components, and support systems and services are excluded
- Civilian Firearms
  - All companies that manufacture firearms and small arms ammunitions for civilian markets are excluded
  - All companies that derive 5% or more revenue from the production and distribution (wholesale or retail) of firearms or small arms ammunition intended for civilian use are excluded
- Genetically Modified Organisms
  - All companies deriving 5% or more revenue from genetic engineering related business activities are excluded
- Nuclear Power
  - All companies generating 5% or more of their total electricity from nuclear power in a given year are excluded

- All companies that have 5% or more of installed capacity attributed to nuclear sources are excluded
- All companies deriving 15% or more revenue from nuclear power-related activities are excluded
- Tightening the **MSCI Climate Change Metrics** methodology for Thermal Coal and adding Fossil Fuel Reserves Ownership and Unconventional Oil and Gas:
  - Thermal Coal
    - All companies deriving any revenue from the mining of thermal coal and its sale to external parties are excluded
    - All companies deriving 5% or more revenue (either reported or estimated) from thermal coal-based power generation are excluded
  - Fossil Fuel Reserves Ownership (New)
    - All companies with evidence of owning proven and probable coal reserves and/or proven oil and natural gas reserves used for energy purposes are excluded
  - Unconventional Oil and Gas (New)
    - All companies deriving any revenue (either reported or estimated) from unconventional oil and gas extraction such as revenues from oil sands, oil shale (kerogen-rich deposits), shale gas, shale oil, coal seam gas, and coal bed methane are excluded
- The following **MSCI Climate Change Metrics** methodology will be removed from the index, as this is now covered under 'Unconventional Oil and gas':
  - Oil sands
    - All companies deriving 5% or more of their total revenue from oil sands extraction, which own oil sands reserves and disclose evidence of deriving revenue from oil sands extraction are excluded

IMBA UK proposes to additionally update the ESG methodology to align with [AMF's policy](#) regulations for clear, accurate and not misleading information disclosure regarding a significant engagement in ESG. The proposed changes are:

- **Minimum Issuer Exclusion Rule**
  - After all of the MSCI ESG screenings are applied, the iBoxx MSCI ESG Liquid Investment Grade Ultrashort indices must exclude at least 20% of

the total number of distinct issuers from the iBoxx Liquid Investment Grade Ultrashort reference indices at every rebalance date, for the respective currency. In the event that the above screenings result in fewer than 20% of issuers being excluded, additional ranking rules are applied to the issuers in the ESG-screened universe, as follows:

1. MSCI ESG rating score (descending)
  2. MSCI ESG controversies score (descending)
- The ranking criteria are applied to each pair of issuers in the order stated above until a difference can be established (i.e. if two issuers have identical ESG rating scores then criteria 2 is applied). With the help of the ranking criteria, an issuer hierarchy can be defined, with the issuer that has the highest ESG rating at the top of the hierarchy
  - For the iBoxx MSCI ESG GBP Liquid Investment Grade Ultrashort Index IMBA UK proposes to rank sub-sovereign issuers that are not covered for MSCI ESG controversies lower than issuers that have identical ESG Rating scores and have ESG controversies coverage
  - Based on the above ranking, issuers will be excluded one by one (starting with the lowest ranked issuer) until the 20% minimum exclusion rule is satisfied. If there is still a tie after these criteria are applied (two or more issuers have the same ESG rating and controversies scores) and the 20% threshold has not yet been met, all these issuers are excluded from the index

## 4. Impact Analysis

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IMBA UK has investigated the potential impact of the updated methodology for the 3 indices:

### iBoxx MSCI ESG EUR Liquid Investment Grade Ultrashort Index

Due to the stricter MSCI Climate Change Metrics, the updated methodology would reduce the number of constituents for the end of August 2021 rebalance from 368 to 354 and the number of distinct issuers from 194 to 185. The updated MSCI ESG Business Involvement Screening would not have an impact on the index for the end of August 2021 rebalance.

The consolidated environmental score would improve from 7.2 to 7.3 and the Greenhouse gas (GHG) intensity (emissions [t] per sales [USD million]) would improve from 67.6 to 54.1.

### iBoxx MSCI ESG GBP Liquid Investment Grade Ultrashort Index

The updated methodology would reduce the number of constituents for the end of August 2021 rebalance from 154 to 152. Due to the stricter MSCI Climate Change Metrics methodology, 3

constituents would be excluded. Due to the update to the MSCI ESG Business Involvement Screening, specifically the updated methodology in relation to Genetically Modified Organisms, 1 bond would become eligible for the index.

The number of distinct issuers would be reduced from 86 to 84. The consolidated environmental score would improve from 6.7 to 6.8 and the Greenhouse gas (GHG) intensity (emissions [t] per sales [USD million]) would improve from 58.0 to 51.3.

#### iBoxx MSCI ESG USD Liquid Investment Grade Ultrashort Index

Due to the stricter MSCI Climate Change Metrics, the updated methodology would reduce the number of constituents for the end of August 2021 rebalance from 512 to 497 and the number of distinct issuers from 184 to 176. The updated MSCI ESG Business Involvement Screening would not have an impact on the index for the end of August 2021 rebalance.

The consolidated environmental score would improve from 6.8 to 6.9 and the Greenhouse gas (GHG) intensity (emissions [t] per sales [USD million]) would improve from 55.2 to 47.3.

For the three above-mentioned indices the minimum issuer exclusion rule would not impact the end of August 2021 rebalance, as more than 20% of all distinct issuers would have already been excluded based on other ESG screening rules.

## **5. Consultation timetable**

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IMBA UK is suggesting a shortened consultation period of 2 weeks to allow for an orderly implementation for the next rebalance date and because the change has already been supported by the main user of the custom indices:

- 29 October 2021 Consultation opens
- 15 November 2021 Consultation closes
- 16 November 2021 IMBA UK reviews stakeholder feedback and a final decision is communicated
- 30 November 2021 Implementation of the ESG methodology changes

## **6. Consultation process**

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The participation of stakeholders in this consultation is important as IMBA UK seeks to gather views on the proposals herein and the suggested timetable for implementation of those proposals. IMBA UK may publish summaries of stakeholders' comments along with IMBA UK's

responses to those comments unless the stakeholder in question expressly requests confidentiality.

To participate in this consultation please respond to IMBA UK Administration Services at [MK-IndexAdminConsultation@ihsmarkit.com](mailto:MK-IndexAdminConsultation@ihsmarkit.com).

Please be advised that all comments will be reviewed and considered before a final decision is made; however, IMBA UK makes no guarantee and is under no obligation to comply with any of the responses. The consultation may result in no changes or outcome of any kind. An announcement will be posted on our website accordingly. IMBA UK reserves the right to make a final decision on the proposal.

## **Key question**

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**Do you have any concerns regarding IMBA UK's proposal or the implementation timeline?**