

An Introduction to the S&P 500 ESG Exclusions II Index

The S&P 500 ESG Exclusions II Index employs a straightforward exclusion methodology that allows investors to eliminate certain types of exposure whilst retaining similar risk-return characteristics to the parent benchmark.

The S&P 500 ESG Exclusions II Index, with its straightforward approach to index construction, includes product involvement screening for controversial weapons, civilian firearms, tobacco and thermal coal as well as norms-based screening that follows the Ten Principles of the UN Global Compact which cover human rights, labour standards, environment and anti-corruption. The S&P 500 ESG Exclusions II Index has delivered a risk-return performance profile that is, statistically, not significantly different to the S&P 500 Index, but at the same time achieves compliance with the typical exclusion-based SRI approaches.

The S&P 500 ESG Exclusions II Index shares similar rules, sector composition and methodology (including the same transparent free-float market-cap weighting scheme) as the S&P 500 Index, which is a broad US equity index containing the largest and most frequently traded equity securities.

A 'Fast Exit' rule in the new index secures a swift response to any severe ESG controversy by quickly removing offenders, thus limiting investors' risks. If a company is reported by RepRisk to have violated the RepRisk Index (RRI) Indicator threshold of 70, the impacted company will be removed from the index with two business days' notice on a best efforts basis from when S&P Dow Jones Indices is notified of the violation. A company removed as a risk will only be considered for addition to the index on any future rebalancing date if its RRI score is below 70 for all days since the previous rebalancing date.

Non-constituents may not be added to the index if their RRI has reached 70 or above any day since the previous rebalancing date.

Key Points

- Compliant with typical exclusion-based SRI approaches¹
- Incorporates ESG data providers Sustainalytics and RepRisk
- Risk-return profile similar to S&P 500
- No strong unintended biases or exposures resulting from exclusions historically exhibited, enabling investors to easily implement and adopt index as ESG-screened benchmark
- Simplicity of methodology makes index suitable as underlying for derivatives and structured products
- Innovative 'Fast Exit' feature allows index to adapt quickly to major controversies

¹ Source: Global Sustainable Investment Alliance.

Figure 1
Index Methodology

Index Name	S&P 500 ESG Exclusions II Index
Parent Index	S&P 500 Index
Parent Index Selection Criteria	The S&P 500 Index tracks the US equity market performance of large cap equity securities.
Weighting Scheme	Free-float market capitalisation
ESG Strategy	Exclusionary
ESG Data Provider	RepRisk and Sustainalytics
Rebalancing Frequency	Quarterly: Mar, Jun, Sep, Dec
Index Ticker	SPXCX2UN

	Exclusion	Criteria — (Defined by ESG Data Provider)	Specific Filter — (Defined by ESG Data Provider)
Exclusion 1	Non-compliance with UN Global Compact Principles ²	UNGC violators	UNGC violators
Exclusion 2	Controversial Weapons ³	Involved with controversial weapons	(i) Internal production or sale of controversial weapons (ii) Ultimate holding company owns > 10% of voting rights of involved company
Exclusion 3	Tobacco	Tobacco producers	0% revenue threshold
Exclusion 4	Thermal Coal	Derive revenues from thermal coal extraction or exploration, or have power generation capacity that utilises thermal coal	(i) >25% revenues from thermal coal extraction (ii) >25% power generation capacity from coal-fired electricity, heat or steam generation capacity/thermal coal electricity production
Exclusion 5	Civilian Firearms	Involved with civilian firearms	(i) Manufactures and sells small arms and assault weapons to civilians and military/law enforcement (ii) Companies with > 10% revenue from small arms and assault weapons sales (iii) > 10% of voting rights of a company are owned by the involved company
Other Features	Fast Exit: if a company is reported by RepRisk to have violated the RepRisk Index (RRI) Indicator threshold of 70, the impacted company will be removed from the index with two business days' notice on a best efforts basis from when S&P Dow Jones Indices is notified of the violation.		

Source: S&P, as of 31 October 2019.

² The Ten Principles of UN Global Compact cover human rights, labour rights, environment, business ethics and anti-corruption.

³ Controversial weapons: Anti-personnel mines, biological and chemical weapons, cluster weapons, depleted uranium, nuclear weapons and white phosphorus (market standard/in line with international conventions).

Figure 2
Characteristics

	S&P 500	S&P 500 ESG Exclusions II
No of Stocks	505 (5 Multiple Listings)	467 (5 Multiple Listings)
Tracking Error (5Y Annualised) vs. S&P 500 (%)	n/a	0 . 66
Fundamentals		
Price/Book 1-Year (Trailing)	3 . 38	3 . 65
P/E incl. Negative (Trailing)	21 . 75	22 . 81
Return on Equity (%)	15 . 54	16 . 01
Annual One-Way Turnover (%)		
2013	1 . 17	1 . 29
2014	0 . 87	1 . 85
2015	1 . 48	1 . 45
2016	1 . 29	1 . 98
2017	1 . 22	2 . 78
2018	0 . 96	0 . 47
ESG Exclusions (# Stocks)		
UNGC Principle Non-Compliant	0	4
Controversial Weapons	0	11
Tobacco	0	2
Thermal Coal	0	18
Civilian Weapons	0	0
Total Excluded in ESG Screened Version	0	35
ESG Exclusions (Weight) (%)		
UNGC Principle Non-Compliant	0 . 00	2 . 32
Controversial Weapons	0 . 00	2 . 65
Tobacco	0 . 00	0 . 83
Thermal Coal	0 . 00	3 . 39
Civilian Weapons	0 . 00	0 . 00
Total Excluded in ESG Screened Version	0 . 00	9 . 21

Source: S&P, as of 31 October 2019. Characteristics are as of the date indicated, are subject to change, and should not be relied upon as current thereafter.

Figure 3
Sector Weights

GICS Sector	S&P 500 (%)	S&P 500 ESG Exclusions II (%)	(+/-) (%)
Information Technology	22.30	24.90	2.61
Health Care	14.03	14.01	-0.02
Financials	12.95	11.40	-1.56
Communication Services	10.42	11.53	1.11
Consumer Discretionary	10.01	10.67	0.66
Industrials	9.24	7.67	-1.57
Consumer Staples	7.42	7.08	-0.33
Energy	4.32	4.71	0.38
Utilities	3.49	1.84	-1.65
Real Estate	3.15	3.30	0.16
Materials	2.67	2.87	0.20

Source: S&P, as of 31 October 2019. Characteristics are as of the date indicated, are subject to change, and should not be relied upon as current thereafter. This information should not be considered a recommendation to invest in a particular sector or to buy or sell any security shown. It is not known whether the sectors or securities shown will be profitable in the future.

Figure 4
Backtested Historical Performance

	Return (%)		Volatility (Annualised, %)		Tracking Error (Annualised, %)
	S&P 500*	S&P 500 ESG Exclusions II	S&P 500	S&P 500 ESG Exclusions II	
1 Month	2.13	2.28	n/a	n/a	0.72
3 Months	2.28	2.17	7.21	7.62	0.76
1 Year	13.63	14.50	17.15	17.25	0.79
3 Years (Annualised)	14.22	14.61	12.07	12.23	0.70
5 Years (Annualised)	10.10	10.19	11.96	12.18	0.66
10 Years (Annualised)	12.99	13.11	12.51	12.67	0.59

Source: S&P, as of 31 October 2019. Past performance is not a guarantee of future results. The inception date for the S&P 500 Exclusions II Index is 26 August 2019. **Results prior to this date are backtested, calculated by using available data at the time in accordance with the Index's current methodology.** *Index returns reflect capital gains and losses, income, and the reinvestment of dividends. **BACKTESTED PERFORMANCE:** This document contains index performance data based on backtesting, i.e. calculations of how the index might have performed prior to launch if it had existed using the same index methodology and based on historical constituents. Backtested performance information is purely hypothetical and is provided in this document solely for information purposes. Backtested performance does not represent actual performance and should not be interpreted as an indication of actual performance.

Figure 5
Example Exclusions

Company Name	Category (which exclusion)	S&P 500 Weight (%)
Berkshire Hathaway B	Thermal Coal	1 . 65
Johnson & Johnson	UNGC principle non-compliant	1 . 38
Wells Fargo & Co	UNGC principle non-compliant	0 . 82
Boeing Co	Controversial Weapons	0 . 72
Philip Morris International	Tobacco	0 . 50
Honeywell Intl Inc	Controversial Weapons	0 . 49
Lockheed Martin	Controversial Weapons	0 . 37
Altria Group Inc	Tobacco	0 . 33
Duke Energy Corp	Thermal Coal	0 . 27
Southern Co	Thermal Coal	0 . 26
Raytheon Co	Controversial Weapons	0 . 23
Northrop Grumman Corp	Controversial Weapons	0 . 22
BlackRock Inc	Controversial Weapons	0 . 21
American Electric Power	Thermal Coal	0 . 18
General Dynamics	Controversial Weapons	0 . 16
Xcel Energy Inc	Thermal Coal	0 . 13
WEC Energy Group Inc	Thermal Coal	0 . 12
T Rowe Price Group Inc	Controversial Weapons	0 . 11
FirstEnergy Corp	Thermal Coal	0 . 10
PPL Corp	Thermal Coal	0 . 10

Source: S&P, as of 31 October 2019. Characteristics are as of the date indicated, are subject to change, and should not be relied upon as current thereafter. This information should not be considered a recommendation to invest in a particular sector or to buy or sell any security shown. It is not known whether the sectors or securities shown will be profitable in the future.

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