

The S&P/BMV Total Mexico ESG Index: A New Benchmark for Sustainability and Investment

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INTRODUCTION

Indices that integrate environmental, social, and governance (ESG) data are moving from the margins to the mainstream, as investors increasingly seek to align their values with their investments. A new type of ESG index is emerging to facilitate this change in Mexico: the [S&P/BMV Total Mexico ESG Index](#). Jointly developed by S&P Dow Jones Indices (S&P DJI) and the Mexican stock exchange (Bolsa Mexicana de Valores [BMV]), this index not only highlights strong ESG companies—as ESG indices have traditionally done—but it also enables investors to allocate to such companies without requiring them to take on major risks relative to the market.

THE EVOLUTION OF ESG INDICES

In 1999, S&P DJI launched the first global ESG index, the [Dow Jones Sustainability™ World Index \(DJSI World\)](#). By including the top 10% of companies, industry by industry, according to their ESG performance, as determined by the Corporate Sustainability Assessment (CSA) conducted by SAM, part of S&P Global,¹ this groundbreaking index encouraged companies to incorporate many ESG factors in their decisions, extending beyond short-term financial considerations.

In the years that followed, other indices, including regional versions of the DJSI World, and local indices, such as the S&P/BMV IPC Sustainable Index, were launched with this same philosophy in mind: to highlight best-in-class companies and thereby inspire companies to improve their ESG approaches in order to qualify for inclusion in these indices.

Though these indices have been successful and have indeed inspired companies to change in positive ways, aspects of their methodologies present challenges for many investors. Some strategies can be too narrow for investors who want to remain broadly diversified. Though many high-conviction investors use the narrow, best-in-class indices for investment, we saw a need from market participants for ESG indices with returns more

¹ For more information on the S&P Global CSA, please refer to <https://www.spglobal.com/esg/csa/about/>.

The philosophy behind the S&P/BMV Total Mexico ESG Index is to maintain breadth...

in line with the broader market, while providing a more sustainable portfolio of companies. An example of an index that launched in 2019 that typifies this investor-oriented methodology is the [S&P 500® ESG Index](#).

...while aligning with the values of sustainability-focused investors.

With the launch of the [S&P/BMV Total Mexico ESG Index](#), Mexico now has an investor-oriented ESG index of its own. This index maintains a large portion of the companies in its underlying index, the [S&P/BMV Total Mexico Index](#), thereby staying broad and diverse while still screening out companies involved in certain business activities and controversies, as well as those with sustainability profiles that run counter to ESG investors' preferences.

HOW THE INDEX WORKS

The philosophy behind the S&P/BMV Total Mexico ESG Index is to maintain broad market exposure while aligning with the values of sustainability-focused investors.

The first step in the methodology is to exclude companies involved in tobacco or controversial weapons, and those with low UNGC scores.

As shown in Exhibit 1, the first step is to exclude companies involved in tobacco or controversial weapons, and those classified as "Non-Compliant" by the United Nations Global Compact (UNGC).² For companies involved in tobacco and controversial weapons, certain maximum revenue thresholds are set, as defined in the [S&P/BMV Indices Methodology](#). If a company generates revenue exceeding these thresholds, it will be excluded at the annual index rebalance that takes place in June each year. Companies with business practices out of alignment with the UNGC are also excluded at the annual rebalance. The exclusion criteria used in Step 1 are provided by Sustainalytics.³

Once these exclusions are implemented, an additional screen is applied using the S&P DJI ESG Scores, an aggregate measure of a company's sustainability.⁴ Companies scoring in the bottom 20% within the S&P/BMV Total Mexico Index are eliminated. Once this is done, the list of companies eligible for the sorting and selection process has been defined.

An additional screen is applied using the S&P DJI ESG Scores.

The final steps are to sort, select, and weight. Companies are sorted by S&P DJI ESG Scores and then selected, working from the top, with the aim of targeting 75% of the original sector's count of companies. The remaining companies are then weighted by their ESG scores, subject to certain weighting constraints defined in the methodology.

² For more information on the UN Global Compact, please refer to <https://www.unglobalcompact.org/>.

³ For more information on Sustainalytics, including the Global Standards Screening Methodology, please refer to <https://www.sustainalytics.com/>.

⁴ See the [FAQ: S&P DJI ESG Scores](#) for more information.

Exhibit 1: S&P/BMV Total Mexico ESG Index Methodology Summary

Objective: To target 75% of the GICS sector stock count of the S&P/BMV Total Mexico Index, using the S&P DJI ESG Scores for the ranking and weighting schemes.

Step 1:

Exclude companies involved in tobacco or controversial weapons, classified as “Non-Compliant.”

Step 2:

Exclude companies with S&P DJI ESG Scores in the bottom 20% of the universe.

Step 3:

Within the index, sort the remaining companies by their S&P DJI ESG Scores within each GICS sector.

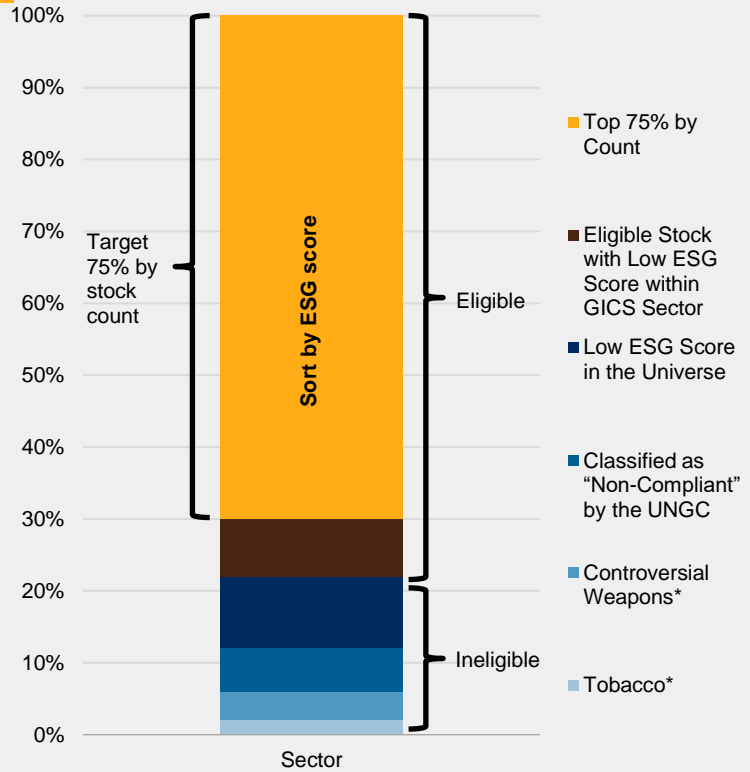
Step 4:

Starting with the company with the highest S&P DJI ESG Score, select companies for inclusion from the top down, targeting 75% of the GICS sector count.

Step 5:

Weight companies by S&P DJI ESG Score.

Index Construction Example



* S&P DJI Level of Involvement threshold as defined in the S&P/BMV Indices Methodology.

** S&P DJI has introduced additional, expanded and revised [exclusions](#) based on a company’s involvement in certain defined business activities. The additional exclusions cover oil sands, small arms and military contracting; the expanded exclusions cover controversial weapons; and the revised exclusions cover tobacco. The previously described methodology changes were effective in conjunction with the June 2022 rebalancing.

Source: S&P Dow Jones Indices LLC. Chart is provided for illustrative purposes.

The result is an index that retained 29 constituents, 51% of the original 56 companies in the S&P/BMV Total Mexico Index as of June 22, 2020, the most recent rebalance.⁵ Representing 61% of the S&P/BMV Total Mexico Index’s market capitalization.

⁵ Coverage in previous years was greatly reduced due to lack of coverage of ESG data.

Exhibit 2: Top 10 Constituents by Weight

CONSTITUENT	GICS SECTOR	SCORE	INDEX WEIGHT (%)	WEIGHT IN BENCHMARK (%)
Cemex SA CPO	Materials	78.6	6.3	3.5
Coca-Cola Femsa SAB de CV UBL	Consumer Staples	77.7	6.2	2.0
Fibra Uno Administracion S.A. de C.V.	Real Estate	82.2	6.2	2.3
Arca Continental, SAB de CV	Consumer Staples	72.4	5.8	1.7
Infraestructura Energetica Nova S.A.B. de C.V.	Utilities	73.5	5.8	1.3
Walmart de Mexico SAB de CV	Consumer Staples	71.6	5.7	11.0
Grupo Televisa SAB CPO	Communication Services	69.4	5.4	2.6
Grupo Financiero Banorte O	Financials	68.0	5.2	7.5
Grupo Aeroportuario del Centro Norte, S.A.B. de C.V.	Industrials	65.6	5.0	1.4
Fomento Economico Mexicano S.A.B. de C.V.	Consumer Staples	57.8	4.6	10.6

Source: S&P Dow Jones Indices LLC. Data as of June 22, 2020. Table is provided for illustrative purposes.

The result is an index that retained 29 constituents, representing 61% of the benchmark's market cap.

The increasing awareness of the relevance of ESG topics for companies and market participants is reflected in the coverage increase over time and historical constituent count (see Exhibit 3).

Exhibit 3: Constituent Count

YEAR	S&P/BMV TOTAL MEXICO INDEX	S&P/BMV TOTAL MEXICO ESG INDEX
2014	67	11
2015	69	13
2016	69	16
2017	77	18
2018	70	28
2019	59	32
2020	56	29

Source: S&P Dow Jones Indices LLC. Data from April 30, 2014, to June 22, 2020. Table is provided for illustrative purposes.

Increasing awareness of ESG topics for is reflected in the coverage increase over time and historical constituent count.

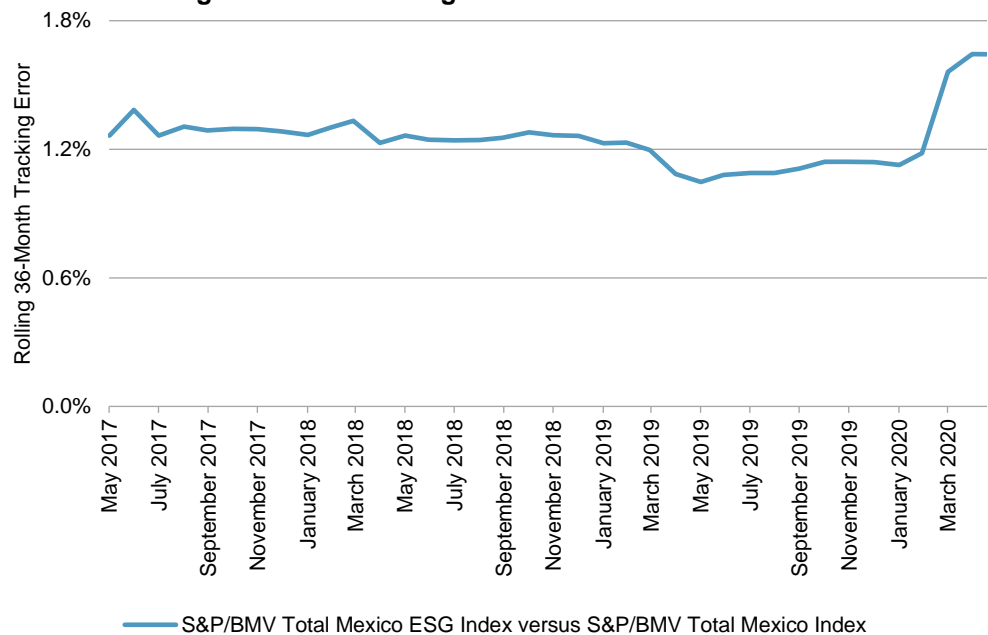
PERFORMANCE OF THE S&P/BMV TOTAL MEXICO ESG INDEX

The appeal of broader ESG indices like the S&P/BMV Total Mexico ESG Index is that they have historically provided an opportunity for similar return to the underlying index—and even the potential for outperformance—without taking on considerable risk associated with narrower ESG indices.

The appeal of a broader ESG index is that they have historically provided similar return to the underlying index.

As seen in Exhibit 4, the index has historically maintained a relatively low tracking error relative to the S&P/BMV Total Mexico Index of about 1.2%. Tracking error increased somewhat in 2020 due to market volatility related to the COVID-19 pandemic.

Exhibit 4: Rolling 36-Month Tracking Error

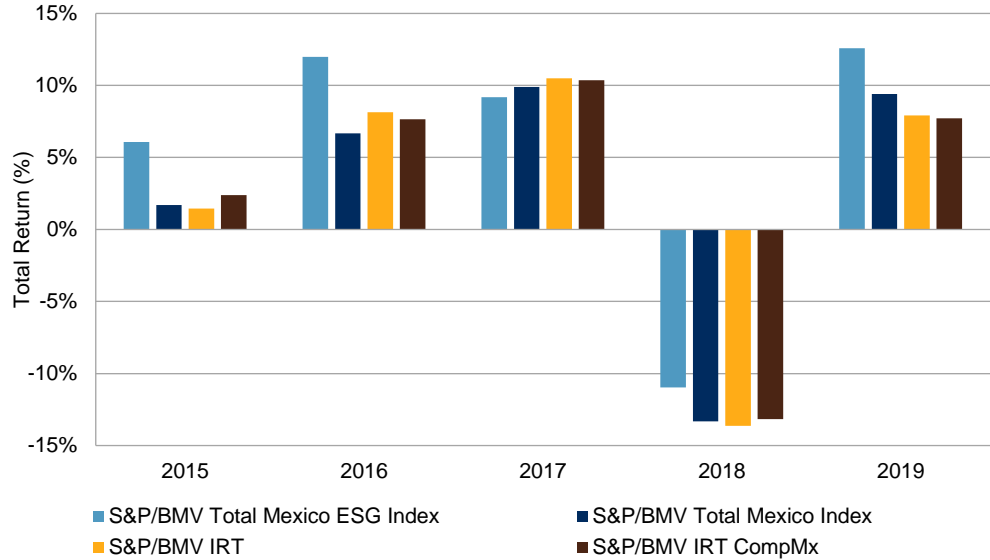


The S&P/BMV Total Mexico ESG Index has maintained a relatively low tracking error relative to the benchmark.

Source: S&P Dow Jones Indices LLC. Data as of June 30, 2020. Index performance based on total return in MXN. Past performance is no guarantee of future results. Chart is provided for illustrative purposes and reflects hypothetical historical performance. Please see the Performance Disclosure at the end of this document for more information regarding the inherent limitations associated with back-tested performance.

Notwithstanding its benchmark-like return, in four of the past five years, the S&P/BMV Total Mexico ESG Index outperformed other major Mexican benchmarks such as the S&P/BMV IRT and S&P/BMV IRT CompMx (see Exhibit 5).

Exhibit 5: Calendar Year Returns



The S&P/BMV Total Mexico ESG Index outperformed other major Mexican benchmarks like the S&P/BMV IRT and S&P/BMV IRT CompMx.

Source: S&P Dow Jones Indices LLC. Data from Dec. 31, 2014, to Dec. 31, 2019. Index performance based on total return in MXN. Past performance is no guarantee of future results. Chart is provided for illustrative purposes and reflects hypothetical historical performance. Please see the Performance Disclosure at the end of this document for more information regarding the inherent limitations associated with back-tested performance.

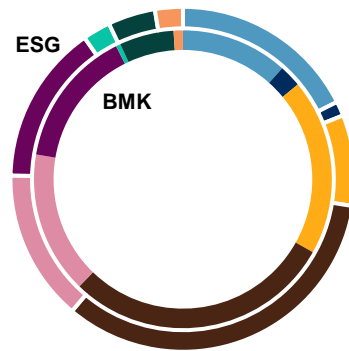
What is the source of this low tracking error and benchmark-like return?

A major factor could be the similarity of the sector compositions of this new ESG index with respect to its underlying index. As Exhibit 6 illustrates, the sector compositions of these indices have been largely in line with each other.

Exhibit 6: Sector Exposure Chart

BMK: S&P/BMV Total Mexico Index

ESG: S&P/BMV Total Mexico ESG Index



SECTOR	SECTOR WEIGHT (%)		
	BMK	ESG	DIFFERENCE
Industrials	12	18	6
Consumer Discretionary	2	1	-1
Communication Services	19	9	-11
Consumer Staples	29	34	5
Financials	15	14	-1
Materials	15	15	0
Health Care	0	3	2
Real Estate	6	4	-1
Utilities	1	3	2

A major factor could be the similarity of the sector compositions of this new ESG index with respect to its underlying index.

Source: S&P Dow Jones Indices LLC. Data as of June 22, 2020. Chart and table are provided for illustrative purposes and reflect hypothetical historical performance. Please see the Performance Disclosure at the end of this document for more information regarding the inherent limitations associated with back-tested performance.

ESG IMPROVEMENT

The aim of excluding certain companies involved in less-sustainable business activities and controversies and those with low S&P DJI ESG Scores is to ensure the selected ESG companies are aligned with a more values-focused portfolio. However, some may wonder how this is measured.

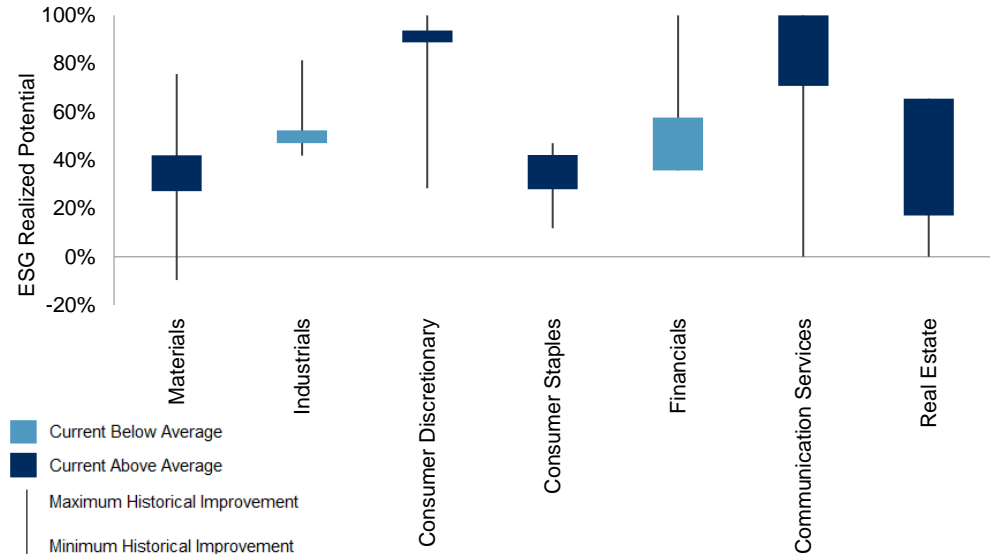
To ensure the ESG index is more values focused, we calculate a composite ESG score to compare it with its underlying index.

One way is to calculate a composite ESG score for the S&P/BMV Total Mexico ESG Index and compare this with the composite score for its underlying index. For the S&P/BMV Total Mexico ESG Index, the composite ESG score was 59.6, which was 17 points higher than the 42.6 composite ESG score of the S&P/BMV Total Mexico Index, representing a 43% improvement.

ESG improvements compared with the benchmark on the sector level over time provide an interesting analysis. For sectors historically represented by more than one company, the average improvement was 48.9% over the seven-year period starting at the 2014 rebalance. It is also worth noting that it is possible to observe a decrease in ESG qualities; this happens when a company with a relatively good ESG score is excluded in the first step. In the S&P/BMV Total Mexico ESG Index, this scenario happened for the Materials sector between 2014 and 2015 (see Exhibit 7).

The composite ESG score for the S&P/BMV Total Mexico ESG Index was 59.6, which was 17 points higher than that of the benchmark.

Exhibit 7: Realized ESG Potential in Sectors



Source: S&P Dow Jones Indices LLC. Data from June 23, 2014, to June 22, 2020, for average sector improvement at rebalance. Past performance is no guarantee of future results. Chart is provided for illustrative purposes and reflects hypothetical historical performance. Please see the Performance Disclosure at the end of this document for more information regarding the inherent limitations associated with back-tested performance.

Over the seven-year period, the average ESG improvement in sectors was 48.9%.

Exhibit 8 shows a few examples of the numerous ways in which the S&P/BMV Total Mexico ESG Index offers enhanced ESG representation. Increased index exposures to each ESG theme in these metrics are calculated using the question-level data in SAM’s CSA.

Exhibit 8: The Benefits of the S&P/BMV Total Mexico ESG Index



Environmental

11% higher exposure to companies conducting and disclosing a materiality analysis that identifies the most important material ESG issues for a company's performance

9% higher exposure to companies that make their direct (Scope 1) and indirect (Scope 2) greenhouse gas emissions publicly available

7% higher exposure to companies that consider and quantify their Scope 3 emissions



Social

18% higher exposure to companies that have a metric to quantitatively measure the benefits from their investments linked to specific employee development programs

13% higher exposure to companies assessing potential human rights issues across their business activities for their employees

8% higher exposure to companies that monitor diversity-related issues, and more specifically female representation across their organization at all levels (including top management positions)



Governance

12% higher exposure to companies that experienced no corruption or bribery cases in the past four fiscal years and that are not currently involved in any ongoing external investigations related to corruption or bribery

9% higher exposure to companies that have a publicly available Supplier Code of Conduct

8% higher exposure to companies that monitor the ratio of actively engaged employees based on scaled employee engagement surveys

Source: SAM, Corporate Sustainability Assessments (2019 methodology year). Metrics calculated using index data as of June 22, 2020, as the percentage difference between the performance of the S&P/BMV Total Mexico ESG Index and the S&P/BMV Total Mexico Index constituents across these metrics, on a weighted average basis. Chart is provided for illustrative purposes.

CONCLUSION

The S&P/BMV Total Mexico ESG Index is a benchmark for a new era in ESG investing, one in which indices are built not just to measure company performance but also to provide model portfolios for broad, diversified investments. As investors use these indices more and more, companies will benefit from their good actions through better brand recognition and through greater investment enabled by these ESG indices.

PERFORMANCE DISCLOSURE

The S&P/BMV Total Mexico ESG Index and S&P/BMV Total Mexico Index were launched June 22, 2020. All information presented prior to an index's Launch Date is hypothetical (back-tested), not actual performance. The back-test calculations are based on the same methodology that was in effect on the index Launch Date. However, when creating back-tested history for periods of market anomalies or other periods that do not reflect the general current market environment, index methodology rules may be relaxed to capture a large enough universe of securities to simulate the target market the index is designed to measure or strategy the index is designed to capture. For example, market capitalization and liquidity thresholds may be reduced. Complete index methodology details are available at www.spdji.com. Past performance of the Index is not an indication of future results. Prospective application of the methodology used to construct the Index may not result in performance commensurate with the back-test returns shown.

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Another limitation of using back-tested information is that the back-tested calculation is generally prepared with the benefit of hindsight. Back-tested information reflects the application of the index methodology and selection of index constituents in hindsight. No hypothetical record can completely account for the impact of financial risk in actual trading. For example, there are numerous factors related to the equities, fixed income, or commodities markets in general which cannot be, and have not been accounted for in the preparation of the index information set forth, all of which can affect actual performance.

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