

## S&P Paris-Aligned & Climate Transition (PACT) Indices Consultation on Eligibility Requirements and Constraints

**AMSTERDAM, JANUARY 28, 2022:** S&P Dow Jones Indices (“S&P DJI”) is conducting a consultation with market participants on potential changes to the S&P Paris-Aligned & Climate Transition (PACT™) Indices, S&P 500 Net Zero 2050 Paris-Aligned Sustainability Screened Index, and Dow Jones Brookfield Global Infrastructure Net Zero 2050 Climate Transition ESG Index.

S&P DJI is proposing to make changes to the eligibility requirements and optimization constraints used in these indices. The proposed changes are detailed below.

### INDEX CONSTRUCTION CONSTRAINTS

S&P DJI is proposing to change the Diversification Relative Weight and Absolute Max Weight constraints from stock level to company level constraints as detailed in the table below. These changes are designed to prevent companies with multiple share classes from being unrepresentatively over/underweighted in the index as a result of the individual classes being considered separately.

Impacted Indices	Proposed Change	Methodology	
		Current	Proposed
S&P Paris-Aligned & Climate Transition (PACT) Indices	Diversification Relative Stock Weight	± 2% from underlying index <b>stock</b> weight	± 2% from underlying index <b>company</b> weight
	Diversification Absolute Max Stock Weight	≤ max(5%, underlying <b>stock</b> weight)	≤ max(5%, underlying <b>company</b> weight)
S&P 500 Net Zero 2050 Paris-Aligned Sustainability Screened Index	Diversification Relative Stock Weight	± 2% from underlying index <b>stock</b> weight	± 2% from underlying index <b>company</b> weight
	Diversification Absolute Max Stock Weight	≤ 20 x <b>stock</b> weight in underlying index	≤ 20 x <b>company</b> weight in underlying index

Please note that the methodology of the Dow Jones Brookfield Global Infrastructure Net Zero 2050 Climate Transition Index already reflects company level constraints. Therefore, these proposed changes are not applicable to it.

### PHYSICAL RISK CONSTRAINT

S&P DJI is proposing to change the Physical Risk Max Weight constraint from a fixed constant of -0.5 to a relative value. This is to ensure that the impact of this constraint remains in line with the index objective related to changes to the climate modelling data sets and hazard models used by Trucost to calculate a company’s physical risk score. In addition, the proposed change would also modify the constraint so that it is applied at the company level instead of the stock level to ensure consistency of approach for companies with multiple share classes. The formula for the Physical Risk Max Stock Weight is as follows:

$$\leq A_i * Parent Weight_i$$

where:

$$A_i = \rho * \frac{PR_i - 100}{PR_i - 10}$$

$PR_i$  = is the Physical Risk score of the company  $i$

(This constraint is only applied to companies with a PR such that  $A_i \leq 4$  and a Physical Risk Score higher than 10)

The table below summarizes the proposed change.

Impacted Indices	Proposed Change	Methodology	
		Current	Proposed
S&P Paris-Aligned & Climate Transition (PACT) Indices <sup>1</sup>	Physical Risk Max Stock Weight	$\rho = -0.5$ Constraint is applied at the <b>stock</b> level	$\rho = \frac{\text{Physical Risk Score 95th percentile} - 10}{\text{Physical Risk Score 95th percentile} - 100}$
S&P 500 Net Zero 2050 Paris-Aligned Sustainability Screened Index			Constraint is applied at the <b>company</b> level

Please note that the methodology of the Dow Jones Brookfield Global Infrastructure Net Zero 2050 Climate Transition Index already reflects the proposed methodology change. Therefore, this proposed change is not applicable to it.

## EXCLUSIONS BASED ON BUSINESS ACTIVITIES

S&P DJI is proposing to increase the level of involvement threshold for Alcoholic Beverages: Production and for Military Contracting: Weapon Related Products and/or Services in the S&P Net Zero 2050 Paris-Aligned Indices as detailed in the table below. These changes are being proposed following feedback that the current exclusions may potentially be too restrictive.

Impacted Indices	Proposed Change	Methodology	
		Current	Proposed
S&P Paris-Aligned & Climate Transition (PACT) Indices:  S&P Net Zero 2050 Paris-Aligned Indices Only	Alcoholic Beverages: Production	level of involvement threshold: >0%	level of involvement threshold: <b>≥5%</b>
	Military Contracting: Weapon Related Products and/or Services	level of involvement threshold: >0%	Two options are being considered. Option 1 – level of involvement threshold: <b>≥5%</b> Option 2 – level of involvement threshold: <b>≥10%</b>

Please note that the methodologies of the S&P 500 Net Zero 2050 Paris-Aligned Sustainability Screened Index and Dow Jones Brookfield Global Infrastructure Net Zero 2050 Climate Transition Index do not reflect these categories of exclusion. Therefore, these proposed changes are not applicable to them.

## OBJECTIVE FUNCTION

S&P DJI is proposing to amend the objective function used for constituent weighting in order to reduce deviations of country and sector level weights in comparison to the parent weights. This change is being proposed for all indices covered by this consultation (i.e. the S&P Paris-Aligned & Climate Transition (PACT) Indices, S&P 500 Net Zero 2050 Paris-Aligned Sustainability Screened Index, and

<sup>1</sup> The S&P UK Net Zero 2050 Climate Transition ESG Index and S&P UK Net Zero 2050 Paris Aligned ESG Index already reflect the proposed methodology, applied at the stock level. For these indices, the constraint would be changed only so that it is applied at the company level.

## CONSULTATION

Dow Jones Brookfield Global Infrastructure Net Zero 2050 Climate Transition ESG Index). The table below summarizes the proposed change.

Methodology	Objective Function
Current	Minimize $\left( \sum \frac{(Parent\ Weight_i - Optimized\ Weight_i)^2}{Parent\ Weight_i} \right)$
Proposed	Minimize $\left( \frac{1}{n} \sum \left[ \frac{(Optimized\ Weight_i - Parent\ Weight_i)^2}{Parent\ Weight_i} \right] + \frac{1}{k} \sum \left[ \frac{(Optimized\ Sector\ Weight_i - Parent\ Sector\ Weight_i)^2}{Parent\ Sector\ Weight_i} \right] + \frac{1}{m} \sum \left[ \frac{(Optimized\ Country\ Weight_i - Parent\ Country\ Weight_i)^2}{Parent\ Country\ Weight_i} \right] \right)$

**IMPACT ANALYSIS**

For an analysis of the impact<sup>2</sup> of the proposed changes, please refer to the file available [here](#).

**IMPLEMENTATION TIMING**

S&P DJI is proposing to implement the previously described methodology changes, if adopted, in conjunction with the upcoming rebalancing, which takes effect prior to the market open on Friday, April 1, 2022. If adopted, the changes will first be visible to clients beginning on Thursday, March 24, 2022.

**QUESTIONS**

Please answer the following questions and provide S&P DJI with the reasoning behind your answers:

1. Do you agree with the proposal to update the Index Construction Constraints as proposed for the S&P Paris-Aligned & Climate Transition (PACT) Indices and the S&P 500 Net Zero 2050 Paris-Aligned Sustainability Screened Index?
2. Do you agree with the proposal to update the Physical Risk Constraint for the S&P Paris-Aligned & Climate Transition (PACT) Indices and the S&P 500 Net Zero 2050 Paris-Aligned Sustainability Screened Index?
3. Do you agree with the proposal to update the Exclusions Based on Business Activities for the S&P Net Zero 2050 Paris-Aligned Indices?
  - Yes, change the level of involvement thresholds for both Alcoholic Beverages: Production and Military Contracting: Weapon Related Products and/or Services to greater than or equal to 5%
  - Yes, change the level of involvement thresholds for Alcoholic Beverages: Production and Military Contracting: Weapon Related Products and/or Services to greater than or equal to 5% and 10%, respectively
  - No, leave the level of involvement thresholds for both Alcoholic Beverages: Production and Military Contracting: Weapon Related Products and/or Services at greater than 0%
4. Do you agree with the proposal to amend the Objective Function for the S&P Paris-Aligned & Climate Transition (PACT) Indices, S&P 500 Net Zero 2050 Paris-Aligned Sustainability Screened Index, and Dow Jones Brookfield Global Infrastructure Net Zero 2050 Climate Transition ESG Index?

<sup>2</sup> The hypothetical impact analysis and statistics apply proposed consultation rules as of the index rebalancing in December 2021.

**CONSULTATION**

5. **If any of the proposed changes are adopted, do you agree with the proposed implementation date?**
6. **Do you have any other comments or feedback regarding the proposed changes outlined above?**

Your participation in this consultation is important as we gather information from various market participants in order to properly evaluate your views and preferences. Please respond to this survey by **February 18, 2022**. After this date, S&P DJI will no longer accept survey responses. Prior to the Index Committee's final review, S&P DJI may request clarifications from respondents as part of that review.

To participate in this consultation, please visit the online survey available [here](#).

For further information about this consultation, please contact S&P Dow Jones Indices at [SPDJI\\_Index\\_Governance@spglobal.com](mailto:SPDJI_Index_Governance@spglobal.com).

*Please be advised that all comments from this consultation will be reviewed and considered before a final decision is made; however, S&P DJI makes no guarantees or is under any obligation to comply with any of the responses. The survey may result in no changes or outcome of any kind. If S&P DJI decides to change the index methodology, an announcement will be posted on our website.*

Thank you for taking the time to complete this survey.

For more information about S&P Dow Jones Indices, please visit [www.spglobal.com/spdji](http://www.spglobal.com/spdji).

## ABOUT S&P DOW JONES INDICES

S&P Dow Jones Indices is the largest global resource for essential index-based concepts, data and research, and home to iconic financial market indicators, such as the S&P 500<sup>®</sup> and the Dow Jones Industrial Average<sup>®</sup>. More assets are invested in products based on our indices than products based on indices from any other provider in the world. Since Charles Dow invented the first index in 1884, S&P DJI has been innovating and developing indices across the spectrum of asset classes helping to define the way investors measure and trade the markets.

S&P Dow Jones Indices is a division of S&P Global (NYSE: SPGI), which provides essential intelligence for individuals, companies and governments to make decisions with confidence. For more information, visit [www.spglobal.com/spdji](http://www.spglobal.com/spdji).

### FOR MORE INFORMATION:

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