and for those regional and international indices which include such markets.

Selection Criteria

The constituents of a country index are selected from the full range of securities available in the market, excluding issues which are either small or highly illiquid. Non-domiciled companies and investment trusts are also excluded from consideration. After the index constituents are chosen, they are reclassified using MSCI's schema of 38 industries and eight economic sectors to facilitate cross-country comparisons.

The process of choosing index constituents from the universe of available securities is consistent among indices. Determining the constituents of an index is an optimization process which involves maximizing float and liquidity, reflecting accurately the market's size and industry profiles, and minimizing cross-ownership.

To reflect accurately country-wide performance, MSCI aims to capture 60% of total market capitalization at both the country and industry level. To reflect local market performance, an index should contain a percentage of the market's overall capitalization sufficient to achieve a high level of tracking. The greater the coverage, however, the greater the risk of including securities which are illiquid or have restricted float. MSCI's 60% coverage target seeks to balance these considerations.

Within the overall target of 60% market coverage, MSCI aims to capture 60% of the capitalization of each industry group, as defined by local practice. MSCI believes this target assures that the index reflects the industry characteristics of the overall market and permits the construction of accurate industry indices.

MSCI may exceed the 60% of market capitalization target in the index for a particular country because, *e.g.*, one or two large companies dominate an industry. Similarly, MSCI may underweight an industry in an index if, *e.g.*, the companies in such industry lack good liquidity and float, or because of extensive cross-ownership.

Liquidity is measured by trading value, as reported by the local exchanges. Trading value is monitored over time to determine "normal" levels exclusive of short-term peaks and troughs. A stock's liquidity is significant not only in absolute terms (*i.e.*, a determination of the market's most actively traded stocks), but also relative to its market capitalization and to average liquidity for the country as a whole.

Float, or the percentage of shares freely tradeable, is one measure of potential short-term supply. Low float raises the risk of insufficient liquidity. MSCI monitors float for every security in its coverage, and low float may exclude a stock from consideration. However, float can be difficult to determine. In some markets good sources generally are not available. In other markets, information on smaller and less prominent issues can be subject to error and time lags. Government ownership and cross-ownership positions can change over time, and are not always made public. Float also tends to be defined differently depending on the source. MSCI seeks to maximize float. As with liquidity, float is an important determinant, but not a hard-and-fast screen, for inclusion of a stock in, or exclusion of a stock from, a particular index.

Cross-ownership occurs when one company has an ownership position in another. In situations where crossownership is substantial, including both companies in an index can skew industry weights, distort country-level valuations and overrepresent buyable opportunities. An integral part of MSCI's country research is identifying cross-ownerships to avoid or minimize inclusion of both companies in an index. Cross-ownership cannot always be avoided, especially in markets where it is prevalent. When MSCI makes exceptions, it seeks to select situations where the constituents operate in different economic sectors, or where the subsidiary company makes only a minor contribution to the parent company's results.

MSCI attempts to meet its 60% coverage target by including a representative sample of large, medium and small capitalization stocks, to capture the sometimes disparate performance of these sectors. In the emerging markets, the liquidity of smaller issues can be a constraint. At the same time, properly representing the lower capitalization end of the market risks overwhelming the index with names. Within these constraints, MSCI strives to include smaller capitalization stocks, provided they exhibit sufficient liquidity.

Calculation Methodology

All MSCI Indices are calculated daily using Laspeyres' concept of a weighted arithmetic average together with the concept of "chain-linking," a classical method of calculating stock market indices. The Laspeyres method weighs stocks in an index by their beginning-ofperiod market capitalization. Share prices are "swept clean" daily and adjusted for any rights issues, stock dividends or splits. The MSCI Indices currently are calculated in local currency and in U.S. dollars, without dividends and with gross dividends reinvested (*e.g.*, before withholding taxes).

In respect of developed markets, MSCI Indices with dividends reinvested constitute an estimate of total return arrived at by reinvesting one-twelfth of the month end yield at every month end.

In respect of emerging markets, MSCI has constructed its indices with dividends reinvested as follows:

- In the period between the ex-date and the date of dividend reinvestment, a dividend receivable is a component of the index return.
- Dividends are deemed received on the payment date.
- To determine the payment date, a fixed time lag is assumed to exist between the ex-date and the payment date. This time lag varies by country, and is determined in accordance with general practices within that market.
- Reinvestment of dividends occurs at the end of the month in which the payment date falls.

Price and Exchange Rates

Prices used to calculate the MSCI Indices are the official exchange closing prices. All prices are taken from the dominant exchange in each market. In countries where there are foreign ownership limits, MSCI uses the price quoted on the official exchange, regardless of whether the limit has been reached.

MSCI uses WM/Reuters Closing Spot Rates for all developed and emerging markets except those in Latin America. The WM/Reuters Closing Spot Rates were established by a committee of investment managers and data providers, including MSCI, whose object was to standardize exchange rates used by the investment community. Exchange rates are taken daily at 4 p.m. London time by the WM Company and are sourced whenever possible from multi-contributor quotes on Reuters. Representative rates are selected for each currency based on a number of "snapshots" of the latest contributed quotations taken from the Reuters service at short intervals around 4 p.m. WM/Reuters provides closing bid and offer rates. MSCI uses these to calculate the mid-point to 5 decimal places.

MSCI continues to monitor exchange rates independently and may, under exceptional circumstances, elect to use an alternative exchange rate if the WM/ Reuters rate is believed not to be representative for a given currency on a