

**STANDARD  
& POOR'S**

# S&P/ASX EMERGING COMPANIES INDEX

INDEX METHODOLOGY



**ASX**  
AUSTRALIAN SECURITIES EXCHANGE

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# Introduction

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In Australia, microcap stocks are defined as those stocks that are generally smaller than the constituents that comprise of the S&P/ASX Small Ordinaries Index, as measured by total market capitalization. The microcap universe is characterized by companies that are smaller, less liquid and relatively under-researched when compared to the broad investable universe of the S&P/ASX 300 Index.

Microcap stocks are, therefore, representative of the segment of the equity market that provides investors with the opportunity to profit from the high growth potential of small and relatively under-researched companies.

The S&P/ASX Emerging Companies Index is the first official benchmark that measures the performance of microcap stocks in the Australian markets. The Index provides investors with a tool to more effectively analyze the characteristics of the microcap segment of the market, thereby allowing a direct comparison to other size segments defined by the S&P/ASX index family.

## **Partnership**

The S&P/ASX index offering was first introduced to the Australian market when the Australian Securities Exchange (ASX) transferred ownership and management of the index business to Standard and Poor's (S&P) on 1 April 2000. Since then, both S&P and ASX have jointly governed the S&P/ASX index suite, ensuring that Australia's indices have been placed at the forefront of the global market. The indices showcase the performance of the Australian equity market and sit alongside other leading international indices, including the S&P 500 and the S&P Global 1200, as some of the world's most transparent and investable equity benchmarks.

## **Highlights**

The S&P/ASX Emerging Companies Index was constructed after a thorough consultation process with many of the leading microcap fund managers in the Australian market. The index portfolio is, therefore, highly representative of the microcap segment and serves as a reliable benchmark for microcap funds in the Australian market.

The S&P/ASX Emerging Companies index has a maximum quota of 200 securities that are selected based on aggregate total market-capitalization and liquidity criteria. The eligibility criteria have been tailored specifically for Australia's microcap universe, recognizing that microcap securities exhibit characteristics that are distinctly different from the larger size segments of the equity market. The eligibility criteria are, therefore,

more customized when compared to the commonly known approach that is adopted for the remainder of the S&P/ASX index family.

The S&P/ASX Emerging Companies index is therefore managed as a discrete portfolio outside the traditional S&P/ASX index hierarchy and results in some overlap with the smaller end of the size spectrum for the S&P/ASX Small Ordinaries index.

### **Index Family**

**S&P/ASX 200.** Upon its introduction in April 2000, the S&P/ASX 200 replaced the All Ordinaries index as the primary gauge for the Australian equity market. The S&P/ASX 200 measures the performance of the 200 largest index-eligible stocks listed on the ASX by float-adjusted market capitalization. Representative, liquid and tradable, it is widely considered as Australia's preeminent benchmark index. The index is float-adjusted, covering approximately 80% of Australian equity market capitalization. Listed companies place immense significance on their membership in the S&P/ASX 200. Inclusion in the index generates significant institutional interest for constituents, and proliferates widespread media and buy/sell side analytical coverage.

**S&P/ASX 20.** The index includes actively traded and highly liquid securities that are among the 20 largest securities listed on the ASX. It is the narrowest capitalization-based index in the S&P/ASX index family, covering approximately 45% of Australian equity market capitalization.

**S&P/ASX 50.** The S&P/ASX 50 is Australia's most prominent large cap equity index, representing 50 of the largest and most liquid index-eligible stocks listed on the ASX by float-adjusted market capitalization. The S&P/ASX 50 represents approximately 65% of Australian equity market capitalization.

**S&P/ASX MidCap 50.** The index is comprised of those companies within the S&P/ASX 100, but not in the S&P/ASX 50. The index is float-adjusted and covers approximately 10% of Australian equity market capitalization.

**S&P/ASX 100.** The S&P/ASX 100 is comprised of the 100 largest index-eligible stocks listed on the ASX by float-adjusted market capitalization. The index is float-adjusted, with securities that are highly liquid and, therefore, institutionally investable. The S&P/ASX 100 represents both the large cap and mid cap component of the S&P/ASX suite of indices and covers approximately 75% of Australian equity market capitalization.

**S&P/ASX 300.** Covering a wide opportunity-set of index constituents, the S&P/ASX 300 is extensively used as a performance benchmark index. The index is highly liquid, float-adjusted and includes up to 300 of Australia's largest securities by float-adjusted market capitalization. The S&P/ASX 300 index includes the large cap, mid cap and small cap components of the S&P/ASX index family. The index covers approximately 81% of Australian equity market capitalization.

**S&P/ASX Small Ordinaries.** The S&P/ASX Small Ordinaries index is used as an institutional benchmark for small cap Australian equity portfolios. The index is

comprised of companies included in the S&P/ASX 300, but not in the S&P/ASX 100. The index covers approximately 7% of Australian equity market capitalization.

**All Ordinaries.** The All Ordinaries index is considered the total market indicator for the Australian equity market. The index is comprised of the 500 largest securities listed on the ASX and the constituents are not screened for liquidity. It is the only index in this family that is not float-adjusted; however, three foreign securities within the index – SGT, TEL and AXN – are float-adjusted.

**S&P/ASX All Australian 50.** Launched in June 2007, the S&P/ASX All Australian 50 is made up of ASX listed securities that have been defined as ‘domestic’ or ‘Australian’ for index purposes. The S&P/ASX All Australian 50 is the Australian component of the S&P Global 1200. It is comprised of highly liquid constituents that are considered to be 50 of the largest index-eligible Australian securities listed on the ASX by float-adjusted market capitalization. The S&P/ASX All Australian 50 follows the same index construction rules that are applied to the S&P/ASX 50. The only exception relates to the index eligibility of securities, with eligibility extending to Australian securities only.

**S&P/ASX All Australian 200.** Launched in June 2007, the S&P/ASX All Australian 200 is made up of ASX listed securities that have been defined as ‘domestic’ or ‘Australian’ for index purposes. The S&P/ASX All Australian 200 is comprised of highly liquid constituents that are considered to be 200 of the largest index-eligible Australian securities listed on the ASX, by float-adjusted market capitalization. The S&P/ASX All Australian 200 follows the same index construction rules that are applied to the S&P/ASX 200. The only exception relates to the index eligibility of securities, with eligibility extending to Australian securities only.

# Eligibility Criteria

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The eligibility criteria for the S&P/ASX Emerging Companies Index are unique in comparison to the general S&P/ASX index family. The S&P/ASX index family is modular in nature with each size component operating as a distinct subset within the S&P/ASX 300, whereas the S&P/ASX Emerging Companies index acts as a discrete portfolio that can overlap with the S&P/ASX Small Ordinaries index.

In order to qualify for inclusion, stocks are first ranked by their total market capitalization to effectively determine each stock's appropriate market capitalization segment. The number of eligible securities is set within a fixed range, with a maximum of 200 securities in the Index. The range of securities that represent the microcap segment was determined through a thorough consultation process, together with a quantitative back testing model. The fixed range and set number of securities has been determined to be an efficient means of representing this market capitalization segment.

Many microcap fund managers accept that they operate within an environment of low liquidity. While this is the case, some liquidity screening does take place for the S&P/ASX Emerging Companies Index so that the benchmark represents a viable opportunity-set for fund managers.

## **Index Eligibility**

The index constituents are drawn from the universe of ordinary and preferred equity stocks listed on the ASX.

## **Eligibility Factors**

**Listing.** Only stocks listed on the Australian Stock Exchange are considered for inclusion in any of the S&P/ASX indices.

**Domicile.** The index draws from the entire universe of ASX listed stocks, which includes both primary and secondary listings on the ASX. A secondary listing occurs when the ASX is not the primary exchange and the stock is listed in multiple markets. This includes foreign-domiciled entities that are incorporated or registered overseas and have their primary listing on an exchange other than the ASX.

**Market Capitalization.** Market capitalization is a critical variable to determine whether a stock falls within the bounds of defined parameters for a particular risk profile. Microcap securities that comprise of the S&P/ASX Emerging Companies Index are defined by a market capitalization range which is set by ranking total market

capitalization for each eligible constituent. Stocks are included in the S&P/ASX Emerging Companies index if they meet minimum and maximum size requirements.

Stocks are included if they fit within the following ranking parameters based upon a six-month average total market capitalization at the rebalancing date:

- < 350<sup>th</sup> and > 600<sup>th</sup>

For example, all else being equal, a stock ranked at 450, based on a six-month average total market capitalization is eligible for inclusion.

Stocks are excluded from the index when they fall outside the following ranking parameters based on six-month total market capitalization at the rebalance date:

- >300<sup>th</sup> and <650<sup>th</sup>

For example, all else being equal, a stock ranked either 280<sup>th</sup> or 700<sup>th</sup>, based on a six-month average total market capitalization, will not be eligible for the index at the rebalancing.

The process above employs a buffer that meets the objective of limiting the extent of portfolio turnover at each rebalancing.

**Liquidity.** Microcap stocks tend to be highly illiquid when compared to other size segments within the equity markets. Stocks eligible for the index if they meet a minimum six-month daily trading average of A\$ 200,000. At the rebalancing, stocks are excluded if the six-month daily average trade minimum is less than A\$ 75,000.

**Shares Outstanding.** When considering the index eligibility of securities for inclusion or promotion into the S&P/ASX indices, the number of index securities under consideration is based upon the latest available ASX quoted securities. For domestic securities this figure is purely based upon the latest available data from the ASX.

Some of the foreign-domiciled securities quote the total number of securities on the ASX that is representative of their global equity capital; whereas other foreign-domiciled securities quote securities on the ASX on a partial basis, which represents only their Australian equity capital. In order to overcome this inconsistency, the S&P/ASX quotes the number of index securities that are represented by CHESS Depository Interests (CDIs) for a foreign entity. The number of CDIs of a foreign entity is representative of the Australian equity capital, thereby allowing the S&P/ASX indices to be increasingly reflective of the Australian market.

### **Timing of Changes**

**Announcements to Market.** Changes to index composition will generally be made two-to-five business days in advance of index implementation of anticipated corporate events whenever practical, bearing in mind that the timing of such events is occasionally uncertain. Announcements will be made outside of trading hours by way of a Press Release, on recognized Australian and international wire services and on the Standard &

Poor's Index Services Web site. Where necessary, a more detailed announcement is made via the *Standard & Poor's Australia Index Alert* FTP site soon after the press release.

*For Press Releases, please visit Standard & Poor's Web site at [www.indices.standardandpoors.com](http://www.indices.standardandpoors.com).*

**Additions.** Between rebalancing dates, an index addition is generally made only if a vacancy is created by an index deletion. Index additions are made according to market size and liquidity. In this case, when a vacancy exists within the portfolio, those eligible securities that rank higher by total market capitalization will be preferred for inclusion.

**Deletions.** Deletions can occur between index rebalancing dates due to acquisitions, mergers and spin-offs or due to suspension or bankruptcies. The decision to remove a stock from the index will be made once there is sufficient evidence that the transaction will be completed. Stocks that are removed due to mergers & acquisitions activity are removed from the index at the cash offer price for cash-only offers. Otherwise the best available price in the market is used.

# Index Construction

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## **Approaches**

The S&P/ASX index series is calculated using a base-weighted aggregate methodology. That means the level of an index reflects the total market value of all the component stocks relative to a particular base period. The total market value of a company is determined by multiplying the price of its stock by the number of shares available after float (IWF) adjustment. An indexed number is used to represent the result of this calculation in order to make the value easier to work with and track over time. It is much easier to graph a chart based on indexed values than one based on actual market values.

## **Index Calculations**

On any given day, the index value is the quotient of the total available market capitalization of the index's constituents and its divisor. Continuity in index values is maintained by adjusting the divisor for all changes in the constituents' share capital after the base date. This includes additions and deletions to the index, rights issues, share buybacks and issuances, spin-offs, and adjustments in availability. The divisor's time series is, in effect, a chronological summary of all changes affecting the base capital of the index. The divisor is adjusted such that the index value at an instant just prior to a change in base capital equals the index value at an instant immediately following that change.

*Please refer to the [Index Mathematics Methodology](#) document for details on index level calculations.*

*Please refer to the [Float Adjustment Methodology](#) document for details on the Investable Weight Factor (IWF) and float-adjustment calculations.*

# Index Maintenance

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Changes in the index level reflect changes in the total market capitalization of the index that are caused by price movements in the market. They do not reflect changes in the market capitalization of the index, or of the individual stocks, that are caused by corporate actions such as dividend payments, stock splits, distributions to shareholders, mergers, or acquisitions. When a corporate action affects the price of a security – such as when the price drops on a special distribution ex-date – the price of the security is adjusted to reflect the ex-date and the index divisor is adjusted to offset any change in the total market value of the index.

When a stock is replaced by another stock, the index divisor is adjusted so that the change in index market value that results from the addition or deletion does not change the index level.

## **Rebalancing**

Rebalancing of the entire S&P Australian index family occurs on a regular basis. Both market capitalization and liquidity are assessed using the previous six months' worth of data to determine index eligibility. Shares and Investable Weight Factors (IWFs) updates are also applied on a regular schedule or when new data becomes available.

*Please refer to the S&P Australia Indices Methodology document for details on index rebalancings.*

**Frequency.** The S&P/ASX Emerging Companies Index is rebalanced semi-annually, with changes taking effect on the third Friday of March and September. The rebalancing reference date is the last Friday prior to March and September.

**Share Updates.** For all Australian indices, the share count all index constituents are updated quarterly and are rounded to the nearest thousand ('000). Issued shares will be updated if the reported outstanding shares differ from total index shares by at least 5% or a market capitalization of A\$ 100 million.

Share updates for foreign-domiciled securities take place annually at the March rebalancing. The update to the number of index shares will only take place when the six-month average of CDIs, as of the March rebalancing, differs from the current index shares by either 5% or a market-cap dollar amount greater than A\$ 100 million. Where CDI information is not supplied to the ASX by the company or the company's share register, estimates for Australian equity capital will be drawn from CHES data and, ultimately, registry-sourced data. Monthly historical data for the number CDI's and

CHESS holdings is available on the ASX Web site at <http://www.asx.com.au/research/indices/index.htm>

### Corporate Actions

Intra quarter share changes are implemented at the effective date or as soon as reliable information is available; however, they will only take place in the following circumstances:

- When market-wide institutional placements are at least 5% of the issued capital of the stock;
- Right's issues, bonus issues and other major corporate actions and;
- Share issues resulting from index companies merging and major off-market buybacks.

Notification of intra quarter changes to the number of issued shares will generally take place three business days prior to the index implementation date. Notification is provided to subscribers of the *Standard & Poor's Index Alert* service, via the relevant FTP site.

In addition to share adjustments, it is necessary to monitor any corporate action that could have a pricing effect on the security and a market capitalization change to the index. Therefore adjustments must be made in relation to company additions and deletions, stock splits, special dividends, and stock price adjustments due to restructurings or spin-offs. Some corporate actions, such as stock splits and special dividends, require simple changes in the common shares outstanding and the stock prices of the companies in the index. Other corporate actions, such as share issuances, change the market value of an index and require an index divisor adjustment to prevent the value of the index from changing.

The following table summarizes the types of index maintenance adjustments and indicates whether a divisor adjustment is required.

### Corporate Actions and the Effect on the Divisor

Events	Index Treatment	Divisor Adjustment Required
Cash Dividend	Applied only to total return indices	No
Special Cash Dividend	Dividend announced as "Special Dividend".	Yes
Stock dividend and/or split	Shares are multiplied by and price is divided by the split factor	No
Stock dividend from class A shares into existing class B shares, both of which are included in the index	Adjustment for price of A; adjustment for shares in B	Yes

### Corporate Actions and the Effect on the Divisor (cont'd)

Events	Index Treatment	Divisor Adjustment Required
Stock dividend of different class, same company and is not included in the index	Price adjustment	Yes
Reverse Split	Adjustment for price and shares	No
Rights offering	Adjustment for price and shares	Yes
Rights offering for a new line	Adjustment for price	Yes
Spin off	Adjustment for price	Yes
New share issuance	Adjustment for shares	Yes
Reduction of capital	Share adjustment	Yes
New addition to index	Share adjustment	Yes
Deletion from index	Share adjustment	Yes
Merger (acquisition by index company for stock)	Share increase	Yes
Warrant conversion into shares	Share increase	Yes

### Base Date

The base date for the S&P/ASX Emerging Companies Index is 31 December 2003, with a base value of 1000.

### Investable Weight Factor (IWF)

Investable Weight Factor =  $1 - \text{Sum of the \% held by strategic shareholders who possess 5\% or more of issued shares.}$

All issues in the S&P/ASX indices – with the exception of the All Ordinaries – are assigned a float-adjustment factor, called an Investable Weight Factor (IWF). The IWF ranges between 0 and 1 and is an adjustment factor that accounts for the publicly available shares of a company. Each company's adjusted market capitalization determines its relative weight in the index.

Standard & Poor's identifies the following shareholders whose holdings are considered to be control blocks and are subject to float adjustment:

1. Government and government agencies;
2. Controlling and strategic shareholders/partners;
3. Any other entities or individuals which hold more than 5%; excluding insurance companies, securities companies and investment funds;
4. Other restricted portions such as treasury stocks.

IWFs are reviewed annually as part of the March quarterly review. However, any event that alters the float of a security in excess of 5% will be implemented as soon as practicable by an adjustment to the IWF.

*Please refer to the Float Adjustment Methodology document for details on the Investable Weight Factor (IWF) and float-adjustment calculations.*

## Index Data

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Both a price return and a total return (accumulation) index series are calculated for all S&P/ASX Emerging Companies index. Cash dividends are applied on the ex-date of the dividend (Dividend franking credits are not included in the total return calculations).

*Please refer to the Index Mathematics Methodology document for details on price and total return calculations.*

# Index Governance

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## **Index Committee**

Each of Standard & Poor's global indices is the responsibility of an Index Committee that monitors overall policy guidelines and methodologies, as well as additions to and deletions from these indices. Standard & Poor's chairs the S&P/ASX Index Committee, which is comprised of five members, representing both Standard & Poor's and the Australian Stock Exchange.

Decisions made by the Index Committee include all matters relating to index construction and maintenance. The Index Committee meets regularly to review market developments and convenes as needed to address major corporate actions.

It is the sole responsibility of the Index Committee to decide on all matters relating to methodology, maintenance, constituent selection and index procedures. The Index Committee makes decisions based on all publicly available information and discussions are kept confidential to avoid any unnecessary impact on market trading.

# Index Policy

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## **Announcements**

Changes to the indices are generally announced two-to-five business days in advance of index implementation whenever practical, bearing in mind that the timing of such events is occasionally uncertain. Announcements will be made outside of trading hours by way of a Press Release, on recognized Australian and international wire services and on the Standard & Poor's Index Services Web site at [www.standardandpoors.com.au](http://www.standardandpoors.com.au). Where necessary, a more detailed announcement is made via the *Standard & Poor's Australia Index Alert* FTP site soon after the press release.

Notification of intra quarter changes to the number of issued shares will generally take place three business days prior to the index implementation date, where possible. Notification is provided to subscribers of the *Standard & Poor's Index Alert* service, via the relevant FTP site.

## **Holiday Schedule**

The S&P/ASX indices are calculated on all business days, this is inclusive of state public holidays. The exchange is closed for trading on national public holidays; indices are not calculated on those days.

## **Recalculation Policy**

Standard & Poor's attempts to avoid incorrect data that affects the indices on a best-efforts basis. Incorrect share calculations and corporate actions are corrected immediately. However, index values are typically not corrected retroactively.

## **Real-Time Calculation**

Real-Time, intra-day, index calculations are executed for 22 S&P/ASX price indices, with index values updated every 30 seconds as constituent prices change throughout the course of the day.

## **Index Precision**

The level of precision for index calculation is as follows:

- Index values are published rounded to two decimal places.
- Share prices are rounded to six decimal places.
- Shares outstanding are expressed in units.
- Investable Weight Factors are rounded to four decimal places.
- Market capitalization is stated to four decimal places.
- Index values are calculated to 14 decimal places.

# Index Dissemination

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Historical index returns are available through Standard & Poor's index data group for subscription via FTP.

## **Tickers**

Daily index values, corporate actions, index weights and portfolios can be received via Standard & Poor's FTP site by subscription. Daily index values can also be viewed on Bloomberg, Reuters and IRESS. The tickers for the primary indices are as below.

<b>Index</b>	<b>Bloomberg</b>	<b>Reuters</b>
S&P/ASX Emerging Companies Index (Price Return)	SPAXEC	.AXEMI
S&P/ASX Emerging Companies Index (Total Return)	SPAXECT	.AXEMIA

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