

**STANDARD
& POOR'S**

S&P CNX SHARIAH INDICES

INDEX METHODOLOGY

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Introduction

In 2006, Standard & Poor's introduced the S&P Shariah Indices. Shariah is Islamic canonical law, which observant Muslims adhere to in their daily lives. Shariah has certain strictures regarding finance and commercial activities permitted for Muslims. Over the last few years, the demand for Shariah compliant financial products has increased.

Recognizing the need for such indices, which are a real gauge of the Indian equity markets and well-established standards, Standard & Poor's and India Index Services & Products Ltd. (IISL) have partnered to bring two major Shariah indices to the Indian market. Shariah screens have been applied to two headline indices – the S&P CNX 500 and the S&P CNX Nifty. The results are the S&P CNX 500 Shariah and the S&P CNX Nifty Shariah.

Shariah Screening

Standard & Poor's has contracted with Ratings Intelligence Partners (RI) to provide the Shariah screens and filter the stocks based on these screens. Ratings Intelligence Partners is a London/Kuwait-based consulting company specializing in solutions for the global Islamic investment market. Its team consists of qualified Islamic researchers who work directly with a Shariah Supervisory Board. It is continually working with regional banks to create Shariah-compliant equity products and expand investment offerings.

RI works with a Shariah Supervisory Board, which is a board of Islamic scholars serving to interpret business issues and recommend actions related to business decisions for the indices. The members are:

- Dr. Muhammad Ali Elgari – PhD in Economics from the University of California, U.S.A.
- Dr. Abdul Sattar Abu Ghuddah – PhD in Islamic Law from Al Azhar University, Cairo, Egypt.
- Dr. Nazih Hammad – PhD in Islamic Law from the University of Cairo, Egypt.
- Dr. Mohammad Amin Ali-Qattan – PhD in Islamic Banking, University of Birmingham, United Kingdom.

Highlights

- Leading equity indices screened for Shariah compliance
- All indices are liquid and investable
- Shariah compliance is as per the strictest standards observed by Middle Eastern countries
- Indices are maintained for compliance on a periodic basis

Index Family

S&P CNX Nifty Shariah. Based on the premier market bellwether for India, the S&P CNX Nifty, the current constituents of the index are screened for Shariah compliance. Those that are compliant form the S&P CNX Nifty Shariah. The resulting index performance closely tracks the performance of the parent index. The Nifty includes the largest and most liquid companies listed on the National Stock Exchange.

S&P CNX 500 Shariah. The complete benchmark for the Indian stock market, the S&P CNX 500 covers more than 90% of the total market capitalization and more than 80% of total traded volume on the National Stock Exchange. The current constituents of the index are screened for Shariah compliance. The resulting compliant stocks form the S&P CNX 500 Shariah, which closely tracks the performance of the parent index.

Representation

All underlying stocks are representative of the Indian equity market, while remaining highly liquid and investable. Each Shariah compliant index typically covers over 60% of the market capitalization of the parent index, though this can vary depending on the number of companies found to be compliant. Historical performance analysis, however, indicates that there is a high level of correlation between the underlying indices and the Shariah compliant indices.

Eligibility Criteria

Sector-Based Screens

Business activities related to the following are excluded:

1. Pork
2. Alcohol
3. Gambling
4. Financials
5. Advertising and Media (newspapers are allowed, sub-industries are analyzed individually)
6. Pornography
7. Tobacco
8. Trading of gold and silver as cash on deferred basis

During the selection process, each company's audited annual report is reviewed to ensure that the company is not involved in any non-Shariah compliant activities. Those that are found to be non-compliant are screened out. The above industries are not considered Islamic and would not be appropriate for investment for observant Muslims.

Accounting-Based Screens

After removing companies with non-compliant business activities, the rest of the companies are examined for compliance in financial ratios, as certain ratios may violate compliance measurements. Three areas of focus are leverage, cash, and the share of revenues derived from non-compliant activities. All of these are subject to evaluation on an ongoing basis.

Leverage Compliance. This compliance is measured as:

Debt / Market Value of Equity (12 Month average) < 33 %;

Cash Compliance. There are compliances with reference to cash holdings. These are:

Accounts Receivables / Market value of Equity (12 Month average) < 49 %;

(Cash + Interest Bearing Securities) / Market value of Equity (12 Month average) <33%;

Revenue Share from Non-Compliant Activities. In certain cases, revenues from non-compliant activities are permissible, if they comply with the following threshold:

$(\text{Non-Permissible Income other than Interest Income}) / \text{Revenue} < 5\%$

Dividend Purification Ratio. This ratio is provided to investors for purification purposes, it is calculated as:

$\text{Dividends} * (\text{Non Permissible Revenue} / \text{Total Revenue})$

Index Eligibility

The stocks are, first, constituents of the underlying indices. They are, then, screened for Shariah compliance. Only those stocks that are compliant remain in the Shariah compliant indices.

For details on the eligibility requirements for underlying indices please refer to their respective methodology documents.

Eligibility Factors

Each of the underlying indices has its own eligibility criteria.

For a complete list of eligibility criteria for the underlying indices, please refer to their respective methodology documents.

Timing of Changes

In general, additions are made to the Shariah indices once a month, typically the third Friday of the month, after the addition to the underlying index, if the stock is found compliant by the Shariah board. Index deletions may also occur at that time, if a constituent is deemed no longer compliant by the Shariah board. Other deletions may occur during the month if a stock is being deleted from the underlying index. Such deletions will occur at the same time as the deletion from the parent index.

Additions. Once an announcement is made of the impending addition to an underlying index, RI will screen it for compliance. If the stock is found to be compliant, after approval by the Shariah board, it will be added to the respective Shariah index. RI will also regularly monitor the existing non-compliant stocks of the underlying index. If any of these stocks become compliant because of changes in financial ratios or changes in business activity due to mergers or restructuring, it will be added to the Shariah index with due notice to clients.

Deletions. All deletions from the parent index will be deleted from the Shariah compliant index on the same day. RI will also conduct an ongoing review of existing Shariah index constituents for continued inclusion in the relevant index.

Additions and deletions to the index, which occur due to ongoing reviews and changes in compliance, are done on the third Friday of each month with due advance notice to clients.

Index Construction

Approaches

The S&P Shariah Indices are calculated using a base-weighted aggregate methodology. This means the level of an index reflects the total float-adjusted market value of all of 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 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.

On any given day, the index value is the quotient of the total available market capitalization of its 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, and spin-offs. 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 value at an instant immediately following that change.

Index Maintenance

Constituents of the S&P CNX Shariah Indices are also constituents of the underlying S&P CNX Indices. As such, specific changes to index constituents – such as share changes, IWF changes, dividend distributions, price adjustments, etc. – will follow the policy of the respective parent index.

Changes in the index level reflect changes in the total market capitalization of the index that are caused by stock 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 on 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 the change in index market value that results from the addition or deletion does not change the index level.

Corporate Actions

Maintaining the S&P CNX Shariah indices includes monitoring and completing the adjustments for company additions and deletions, share changes, stock splits, stock dividends, and stock price adjustments due to restructurings or spin-offs. Some corporate actions, such as stock splits and stock 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.

Adjusting the index divisor for a change in market value leaves the value of the index unaffected by the corporate action. This helps keep the value of the index accurate as a barometer of stock market performance, and ensures that the movement of the index does not reflect the corporate actions of the companies in it. Divisor adjustments are made after the close of trading and after the calculation of the closing value of the index. Any change in the index divisor also affects the corresponding sub-indices and divisors. Each sub-index is maintained in the same manner as the headline index.

Corporate actions such as splits, stock dividends, spin-offs, rights offerings, and share changes are applied on the ex-date.

Compliance Audit

As soon as any new information regarding a constituent company is collected, compliance is reviewed. RI provides the compliance data to Standard & Poor's via a monthly compliance report. A daily screening report is checked by RI and provided to the Shariah supervisory board. A member of the Shariah board signs off on a monthly basis. Standard & Poor's reviews the monthly report and, accordingly, removes any existing constituents for non-compliance.

Currency of Calculation

The indices are calculated in Indian rupees.

Base Date

The indices have a base date of January 1, 2007 with history back to that date, as well.

Investable Weight Factor (IWF)

All issues in the S&P CNX Shariah indices are assigned a float 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. The company's adjusted market capitalization determines an equity issue's relative weight in the index. The IWF is exactly the same as it is for the constituents in the underlying indices.

Please refer to the Float Adjustment methodology document for general information on float adjustment and Investable Weight Factors.

Please refer to the individual regional index methodologies for further treatment of Investable Weight Factors by geographic area.

Index Governance

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. The S&P CNX Index Committee is jointly composed of Standard & Poor's and IISL representatives.

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.

Shariah Expertise

Standard & Poor's has contracted with Ratings Intelligence Partners which is a London/Kuwait based Shariah consultancy. The company was established in 2000 to develop leading-edge solutions for the global Islamic investment market. Its current focus is on consulting leading hedge fund organizations in the implementation of Shariah compliant hedge funds. The emphasis is presently on equity long/short strategies; however, work is underway to expand the process to other strategies, subject to Shariah approval.

The Shariah Supervisory Board

Dr. Muhammad Ali El-Gari.

- PhD in Economics from the University of California, California, United States.
- Professor of Islamic Economics, King Abdul Aziz University, Jeddah, Saudi Arabia.
- Former Director, Centre for Research in Islamic Economics, King Abdulaziz University.
- Member, Academic Committee, Islamic Development Bank, Jeddah.
- Member of Islamic Fiqh¹ Academy, Jeddah.
- Editor, Review of Islamic Economics, London (Journal of the International Association of Islamic Economics).
- Shariah board member for National Commercial Bank (Saudi Arabia), Citi Islamic Investment Bank (Saudi Arabia), Saudi American Bank, Saudi British Bank and Dow Jones Islamic Index (United States).

Dr. Abdul Sattar Abu Ghuddah.

- Holds Licenses in Islamic Law from Damascus University, Syria.
- PhD in Islamic Law from Al Azhar University, Cairo, Egypt.
- MSc in Islamic Law and Hadith.
- Shariah advisor of several Islamic financial, banking and governmental institutions.
- Advisor for Islamic Law Encyclopedia (Kuwait Awqaf Ministry).
- Shariah board member for Al-Baraka Islamic Investment Co (Saudi Arabia), Dow Jones Islamic Index (United States), Al-Tawfeek Co (Saudi Arabia) and SAMBA (Riyadh).

Dr. Nazih Hammad.

- PhD in Islamic Law from the University of Cairo, Egypt.
- Former Professor at the college of Shariah, Um Alqura University, Makkah Al Mukkarmah for 17 years.
- Member of the Islamic Fiqh¹ Academy, Jeddah, Saudi Arabia (Organization of Islamic Countries).
- Graduate of the University of Damascus, Syria.
- Shariah board member for Citi Islamic Investment Bank (Bahrain), Permal Asset Management (United States).

Dr. Mohammad Amin Ali Qattan.

- PhD in Islamic Banking from Birmingham University, UK and BA in Islamic Economics from Saudi Arabia.
- Director of the Islamic Economics Unit, College of Business Administration, Kuwait University.
- Faculty member at the American University of Cairo in 2006, Lecturer at the College of Trading Studies in Kuwait.
- Author and presenter of many articles and books in Islamic Economics, accredited trainer in the Islamic business field by many institutions inside and outside Kuwait.
- Member of Shari'a Control Committees in many Islamic financial firms in Kuwait, USA, London, Geneva, Kenya and Bahrain.

Index Policy

Announcements

All additions, deletions, share and Investable Weight Factor (IWF) changes are normally announced well ahead of the effective date. These announcements are posted on IISL's Web site and sent to clients by email. Quarterly changes are also announced a few days before the effective date.

Holiday Schedule

Single country indices follow the national holiday schedule in the country.

A complete holiday schedule for the year is available on the Standard & Poor's Web site at www.indices.standardandpoors.com.

Recalculation Policy

Incorrect share calculations and corporate actions are corrected immediately. However, index values are typically not corrected retroactively.

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

Index Dissemination

Tickers

Daily index values, corporate actions, index weights and portfolios can be received via Standard & Poor's FTP site. Additionally, daily index values can be viewed on Bloomberg and Reuters. The tickers are as below:

Tickers

S&P CNX Shariah Indices	Bloomberg	Reuters
S&P CNX Nifty Shariah Index	INSHNIFT	.SPSHNSI
S&P CNX 500 Shariah Index	INSHC500	.SPSHCNF

FTP

Daily stock level and index data are available via FTP on subscription.

For further information, please refer to IISL's Web site at http://www.nseindia.com/content/indices/ind_majorindices.htm or Standard & Poor's Web site at www.indices.standardandpoors.com.

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