Zug, November 14, 2024

Market Consultation on proposed enhancements to the DAX ESG Target

Dear Sir and Madam,

STOXX Ltd. has decided to conduct a market consultation on proposed enhancements to the DAX ESG Target.

The market consultation may or may not lead to changes in the index methodology.

Process and Timeline

STOXX invites relevant stakeholders and interested third parties to submit responses via this online survey or to consultation@stoxx.com.

The consultation is open to all market participants until November 29, 2024.

STOXX intends to announce the results of the market consultation, as well as an announcement about potential changes to the index methodology, by December 6, 2024.

STOXX intends to implement the potential changes resulting from this consultation as of the quarterly index review effective date in March 2025.

Motivation for the Market Consultation

The DAX ESG Target index aims to replicate the performance of the DAX, while incorporating ESG criteria in the selection and weighting process. In the past, exclusions due to ESG screens have accounted for a majority of the ex-ante tracking error budget, leaving little room for ESG improvement and leading to continued breaches of the tracking error constraint. The free tracking error budget has further tightened since the upper limit for single stocks weights has remained at 10% in DAX ESG Target after the cap limit increase in DAX to 15% as of March 15, 2024. STOXX seeks to consult on methodology enhancements that allow for meaningful improvements of the index' ESG profile, while maintaining a low tracking error compared to the DAX.

Furthermore, the ESMA fund names guideline requires funds (and in turn the indices they track) to adhere to specific minimum criteria related to exclusionary screens and sustainable investments. STOXX therefore seeks to consult on methodology enhancements that align the DAX ESG Target with these requirements.

Lastly, STOXX seeks feedback on a switch to Sustainalytics ESG Risk Scores as Sustainalytics has decided to decommission their legacy ESG scores in December 2024.

Proposed Treatments/Amendments

STOXX is looking to enhance the methodology of the DAX ESG Target with the following proposed changes to existing index rules:

Table 1: Proposed changes to the DAX ESG Target selection process

	Current Methodology	Proposed Methodology
(a) Decrease of the thermal coal extraction revenue threshold	**Thermal coal:** STOXX excludes companies that Sustainalytics identifies as meeting one or more of the following criteria: ▪ **>5%** of revenues from thermal coal extraction (including thermal coal mining and exploration) ▪ >5% power generation capacity: coal-fired electricity, heat or steam generation/thermal coal electricity production (including utilities that own/operate coal-fired power plants)	**Thermal coal:** STOXX excludes companies that Sustainalytics identifies as meeting one or more of the following criteria: ▪ **>1%** of revenues from thermal coal extraction (including thermal coal mining and exploration) ▪ >5% power generation capacity: coal-fired electricity, heat or steam generation/thermal coal electricity production (including utilities that own/operate coal-fired power plants)
(b) Introduction of an oil & gas exclusionary screen		**Oil and Gas:** STOXX excludes companies that Sustainalytics identifies as deriving: ▪ >10% of revenues from oil and gas exploration, production, refining, transportation and/or storage. This category evaluates oil and gas related activities' share of total company's revenue. Assessments are made for producers, refiners, transporters, and companies engaged in storage (proxy: revenues).
(c) Introduction of a fossil fuel power generation exclusionary screen		**Fossil Fuel Power Generation:** STOXX excludes companies that Sustainalytics identifies as deriving: ▪ >50% of revenues from generating electricity from oil and/or gas (proxy: generating capacity) and coal-fired electricity, heat or steam generation capacity / thermal coal electricity production (including utilities that own/operates coal-fired power plants).

(d) Change of the replacement process for companies that are screened out	DAX companies that have been excluded as described in Step 1 will be replaced in the following manner: The companies still in the HDAX following screening as described in Step 1 are then ranked from high to low in terms of their free-float market capitalization (as reported in the most recent DAX selection indices selection list). In addition, the ESG score for each constituent is displayed. Starting with the largest companies (measured in terms of their free-float market capitalization), companies are then included in the index if they have the same or a better ESG ranking than the DAX Regular Exit candidate rank for free-float market capitalization (see section 7.1.2). The ESG ranking is calculated using the composition of the HDAX after all exclusions have been omitted. This process is repeated until the number of DAX ESG Target constituents matches the number of DAX constituents.	DAX companies that have been excluded as described in Step 1 will be replaced in the following manner: The companies still in the HDAX following screening as described in Step 1 are then ranked from high to low in terms of their free-float market capitalization (as reported in the most recent DAX selection indices selection list). Starting with the largest companies (measured in terms of their free-float market capitalization), companies are then included in the index. This process is repeated until the number of DAX ESG Target constituents matches the number of DAX constituents.

Table 2: Proposed changes to the DAX ESG Target weighting process		
	Current Methodology	**Proposed Methodology**
(a) Change of the objective function from maximizing the portfolio's ESG score to minimizing the portfolio's predicted tracking error	Weightings are derived using an optimization process that aims to maximize the portfolio's ESG score (as measured by Sustainalytics' ESG scores). The following constraints are applied:	Weightings are derived using an optimization process that aims to minimize the ex-ante tracking error subject to:
(b) Increase of the single stock weighting constraint	$MAX(bmin,b/2) < w<MIN(10*b,b+2\%,\mathbf{10\%})$	$MAX(bmin,b/2) < w<MIN(10*b,b+2\%,\mathbf{15\%})$
(c) Switch from the predicted tracking error constraint to an ESG Risk Rating constraint	• Tracking error: Predicted tracking error <1.5% [...] Where infeasibilities arise, the tracking error, soft turnover and supersector active exposures constraints can all be potentially violated if necessary to find a solution that minimizes the aggregate violations.	• ESG risk rating: The weighted average ESG Risk rating must be lower or equal to the benchmark [...] Where infeasibilities arise, the soft turnover and supersector active exposures constraints can all be potentially violated if necessary to find a solution that minimizes the aggregate violations.

(d) Introduction of a minimum sustainable investments threshold		Sustainable Investment (SI) commitment: a minimum of 20% of the index weight is defined as Sustainable Investment. Clarity AI's Sustainable Investment framework is used to evaluate companies' sustainability objectives and their environmental and social contributions. The companies in the selection have to satisfy all of the criteria below in order to be considered towards the SI commitment of the index: » companies identified as having positive contributions according to Clarity AI's Sustainable Investment framework » companies that are non-compliant according to the Global Standards Screening assessment are not eligible » companies that are not involved in Controversial Weapons, according to the definitions above » companies with High or Severe Sustainalytics Controversy Ratings are not eligible » companies with High or Severe Sustainalytics Carbon Risk Ratings are not eligible » companies with Product Involvement higher than these thresholds are not eligible for the SI label: - 0% revenues from manufacturing tobacco products - 5% revenues from supplying tobacco-related products/services - 5% revenues from the distribution and/or retail sale of tobacco products - 0% revenues from thermal coal extraction (including thermal coal mining and exploration) Companies with no data in any of the above fields will not be eligible for the SI label.

Affected Indices

DAX ESG Target

Questions

1. Do you agree with the proposed decrease of the thermal coal extraction revenue threshold from >5% to >1% [see table 1 (a)]?
2. Do you agree with the proposed introduction of an oil & gas exclusionary screen that excludes companies that derive >10% of revenues from oil and gas exploration, production, refining, transportation and/or storage [see table 1 (b)]?
3. Do you agree with the proposed introduction of a fossil fuel power generation exclusionary screen that excludes companies that derive >50% of revenues from generating electricity from oil and/or gas and coal-fired electricity, heat or steam generation capacity / thermal coal electricity production [see table 1 (c)]?
4. Do you agree with the proposed change of the replacement process for companies that are screened out by the exclusionary screens [see table 1 (d)]?
5. Do you agree with the proposed change of the objective function from maximizing the portfolio's ESG score to minimizing the portfolio's predicted tracking error [see table 2 (a)]?
6. Do you agree with the proposed increase of the single stock weighting constraint from 10% to 15% [see table 2 (b)]?
7. Do you agree with the proposed switch from the predicted tracking error constraint to an ESG Risk Rating constraint [see table 2 (c)]?
8. Do you agree with the proposed introduction of a minimum sustainable investments threshold of 20% [see table 2 (d)]?

If your answer to any of the above questions is NO, please also kindly explain your reasons behind it.