

# Emerging vs. Developed Markets Classification

## Why it Matters to Investors

- MSCI has been classifying Emerging and Developed markets since the introduction of the MSCI Emerging Markets Index in 1988. The MSCI classification framework is based on an assessment of three dimensions: 1) economic development, 2) size and liquidity of equity markets, 3) market accessibility for foreign investors.
- Why is this important for investors? The misclassification of a market within a global index may significantly increase the cost, tracking error and overall risk of a portfolio tracking the index. A frequent misconception is to equate an advanced economy with an advanced stock market. This may lead to overlooking other important issues such market accessibility.
- Korea, for example, is a fairly developed economy with several world class companies. However, Korea's equity market is not yet at the developed level when objectively compared to the 24 markets that MSCI classifies as developed. Korea, which has been under review by MSCI for developed status for the last 5 years, will only be reclassified when accessibility issues are resolved and following a consultation with investors.

### MSCI Market Classification Framework

The MSCI market classification framework is based on an assessment of three dimensions of a country's market:

- Economic development:** uses Gross National Income (GNI) per capita as published by the World Bank.
- Size and liquidity of its equity markets:** consistent cross country comparison for 77 markets.
- Accessibility for foreign investors:** uses 18 distinct measures such as foreign ownership limits or capital flow restrictions.

### Korea: An Illustration

- Korea meets the economic development and size and liquidity criteria for developed market status. However, it currently fails the accessibility criteria.
- All developed market currencies today are traded 24 hours around the world. In Korea, foreign investors can only trade the local currency during Korean business hours with Korean legal entities. Such restrictions make global portfolio rebalancing difficult and may cause tracking error.
- In Korea, the use of omnibus trading accounts and in-kind transfers, which are commonly used by institutional investors to manage thousands of client accounts, is difficult or prohibited. This results in complex processes for managers and leads to higher costs and fees for the end investor.

### MSCI Developed Markets and Korea

#### Economic Development & Key Market Accessibility Measures

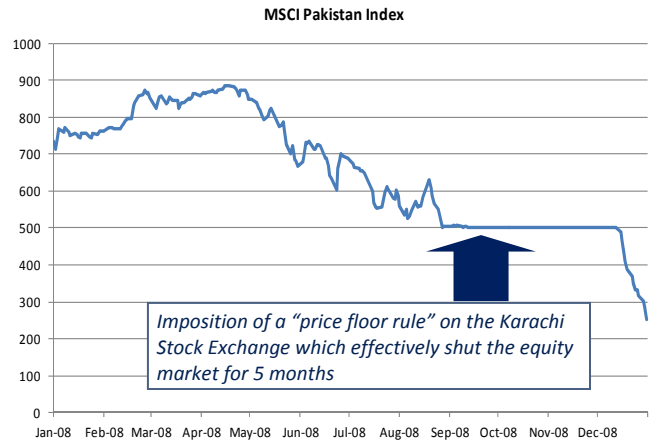
Economic Development		Market Accessibility	
GNI per capita	Country Name	FX convertibility	In-kind transfer/ Omnibus acc.
█	Norway	✓	✓
█	Switzerland	✓	✓
█	Denmark	✓	✓
█	Sweden	✓	✓
█	Netherlands	✓	✓
█	United States	✓	✓
█	Finland	✓	✓
█	Austria	✓	✓
█	Australia	✓	✓
█	Belgium	✓	✓
█	Canada	✓	✓
█	Japan	✓	✓
█	Germany	✓	✓
█	Singapore	✓	✓
█	France	✓	✓
█	Ireland	✓	✓
█	United Kingdom	✓	✓
█	Italy	✓	✓
█	Hong Kong	✓	✓
█	Spain	✓	✓
█	New Zealand	✓	✓
█	Israel	✓	✓
█	Greece	✓	✗
█	Portugal	✓	✓
█	Korea	✗	✗

Source: MSCI, World Bank, as of November 2012

## Managing Risk in Emerging Markets

- Although many emerging markets over the years have improved certain regulations and market practices, in general they are more commonly subject to crises and market disruptions.
- In June of each year, MSCI reviews the classification of the 77 markets it covers. Any change follows extensive consultations with international investors around the world.
- Classification changes may also occur off cycle, if severe market disruptions—such as the introduction of capital flow restrictions—prevent investors from entering or exiting the market.
- For example, MSCI moved Pakistan and Argentina from Emerging to Frontier Markets status and dropped the coverage of Venezuela following major market crises.

### 2008 Performance of the MSCI Pakistan Index



### For over 40 Years MSCI Has Captured the Evolution of Markets in a Timely Manner:

1960s - 1970s Developed Markets		1980s - 1990s Introduction and Expansion of Emerging Markets		2000s Increased Opportunities in GCC and Frontier Markets		
Year	Country	Year	Country	Year	Country	
1969	Australia	1981	Mexico <sup>3</sup>	1990	Indonesia	
	Austria		Finland		Turkey	
	Belgium		New Zealand		Ireland	
	Canada	Argentina	Luxemburg <sup>4</sup>			
	Denmark	1988	Brazil	1993	Colombia	
	France		Chile		India	
	Germany		Jordan		Pakistan	
	Italy		Malaysia		Peru	
	Japan		Philippines		Sri Lanka <sup>5</sup>	
	1972	Netherlands	1989	Thailand	1995	Venezuela <sup>5</sup>
		Norway		Greece		China
		Spain		Korea		Israel
		Sweden	Portugal	Poland		
		Switzerland	Taiwan	South Africa		
		United Kingdom	1996	Russia	Czech Republic	
		United States		Hungary		
1974		Hong Kong		1997	Portugal joins DM	
		Malaysia / Singapore <sup>1</sup>				
		South Africa Gold Mines <sup>2</sup>				
2001	Egypt	2006		Bahrain <sup>8</sup>	2007	Bulgaria
	Morocco		Kuwait <sup>8</sup>	Croatia		
	Greece joins DM		Oman <sup>8</sup>	Estonia		
	2008		Qatar <sup>8</sup>	Saudi Arabia		Kazakhstan
			Bahria joins FM	United Arab Emirates <sup>9</sup>		Romania
		Jordan joins FM		Slovenia		
	2009	Argentina joins FM		Ukraine		
		Trinidad & Tobago <sup>7</sup>		Kenya		
		Jamaica <sup>7</sup>		Mauritius		
		Ghana <sup>7</sup>		Nigeria		
2010	Botswana <sup>7</sup>		Tunisia			
	Bangladesh		Lebanon			
	Bosnia Herzegovina <sup>7</sup>		Sri Lanka joins FM <sup>5</sup>			
2012	Israel joins DM		Vietnam			
	Saudi Arabia discontinued <sup>9</sup>					
	Zimbabwe <sup>7</sup>					
	Saudi Arabia <sup>10</sup>					

<sup>1</sup> Effective 4/30/93, the MSCI Malaysia / Singapore Index became the MSCI Singapore Index. <sup>2</sup> The MSCI South Africa Gold Mines Index was included in the MSCI World Index from 12/2/74 to 3/1/95. <sup>3</sup> On 11/5/81, the MSCI Mexico Index was included in the MSCI World Index and then became part of the MSCI EM Index on 1/1/88. <sup>4</sup> The MSCI Luxembourg Index was discontinued as of the close of 3/29/02. <sup>5</sup> Effective 5/31/01, the MSCI Sri Lanka Index was excluded from the MSCI EM and MSCI ACWI Indices. The MSCI Sri Lanka Index was a stand-alone index until 2007 when it was included in the MSCI FM Index. <sup>6</sup> Effective 5/31/06, the MSCI Venezuela Index was excluded from the MSCI EM and ACWI Indices and then discontinued effective 12/31/07. <sup>7</sup> The MSCI Bosnia Herzegovina, MSCI Botswana, MSCI Ghana, MSCI Jamaica, MSCI Trinidad & Tobago and MSCI Zimbabwe Indices are stand-alone indices that are not currently included in the MSCI FM Index but are under consideration for inclusion. <sup>8</sup> All GCC countries ex Saudi Arabia are part of MSCI FM Index. <sup>9</sup> On 9/30/10, MSCI discontinued the calculation of the MSCI Saudi Arabia Index. <sup>10</sup> On 6/26/2012, MSCI resumed calculation of the stand-alone MSCI Saudi Arabia Index.

Developed Markets
Emerging Markets
Frontier Markets
GCC Countries <sup>8</sup>

Learn more about [MSCI Market Classification: www.msci.com/products/indices/market\\_classification.html](http://www.msci.com/products/indices/market_classification.html)

[www.msci.com](http://www.msci.com) | [clientservice@msci.com](mailto:clientservice@msci.com)

The information contained herein (the "Information") may not be reproduced or disseminated in whole or in part without prior written permission from MSCI. The Information may not be used to verify or correct other data, to create indices, risk models, or analytics, or in connection with issuing, offering, sponsoring, managing or marketing any securities, portfolios, financial products or other investment vehicles. Historical data and analysis should not be taken as an indication or guarantee of any future performance, analysis, forecast or prediction. None of the Information or MSCI index or other product or service constitutes an offer to buy or sell, or a promotion or recommendation of, any security, financial instrument or product or trading strategy. Further, none of the Information or any MSCI index is intended to constitute investment advice or a recommendation to make (or refrain from making) any kind of investment decision and may not be relied on as such. The Information is provided "as is" and the user of the Information assumes the entire risk of any use it may make or permit to be made of the Information. NONE OF MSCI INC. OR ANY OF ITS SUBSIDIARIES OR ITS OR THEIR DIRECT OR INDIRECT SUPPLIERS OR ANY THIRD PARTY INVOLVED IN THE MAKING OR COMPILING OF THE INFORMATION (EACH, AN "MSCI PARTY") MAKES ANY WARRANTIES OR REPRESENTATIONS AND, TO THE MAXIMUM EXTENT PERMITTED BY LAW, EACH MSCI PARTY HEREBY EXPRESSLY DISCLAIMS ALL IMPLIED WARRANTIES, INCLUDING WARRANTIES OF MERCHANTABILITY AND FITNESS FOR A PARTICULAR PURPOSE. WITHOUT LIMITING ANY OF THE FOREGOING AND TO THE MAXIMUM EXTENT PERMITTED BY LAW, IN NO EVENT SHALL ANY OF THE MSCI PARTIES HAVE ANY LIABILITY REGARDING ANY OF THE INFORMATION FOR ANY DIRECT, INDIRECT, SPECIAL, PUNITIVE, CONSEQUENTIAL (INCLUDING LOST PROFITS) OR ANY OTHER DAMAGES EVEN IF NOTIFIED OF THE POSSIBILITY OF SUCH DAMAGES. The foregoing shall not exclude or limit any liability that may not by applicable law be excluded or limited.