

ETF INSIGHTS

US small-cap investing with MSCI Select Filtered Min TE index

Context

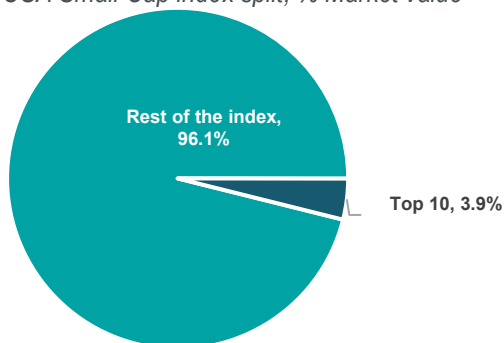
- US small caps provide distinct benefits vs traditional large and mid-cap exposures
- The composition of US small-cap indices is more balanced in terms of sector and top 10 concentration
- The definition of a small-cap investment universe can have a notable impact on the strategy's performance

Key features

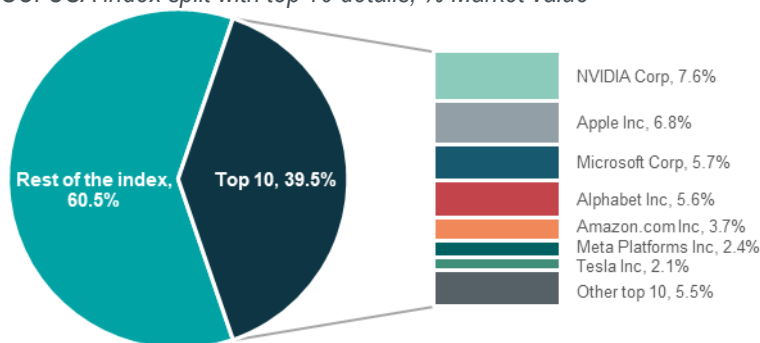
- ESG integration on three levels: business exclusion, ESG score and carbon intensity improvement
- Very limited tracking-error vs standard US small-cap index (0.55% 1-year ex-post)
- Very similar historical performance and volatility figures

US small-cap indices are a lot less concentrated in the top names than their large-cap equivalent

MSCI USA Small Cap index split, % Market value



MSCI USA index split with top 10 details, % Market value



Source: BNP Paribas Asset Management, MSCI as of 31/01/2026. Past performances are not indicative of current or future performance.

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Diversifying US equity exposures through small-cap companies

Investing in US companies with a small market capitalisation can provide distinct benefits over exposure to large and mid-caps: small caps are often at the forefront of innovation and in early stages of the growth cycle. Traditionally, small-cap companies are also more exposed to the shape of the domestic economy: they typically operate in local markets rather than international ones.

That is not to say that they are impervious to political developments such as trade policies. Initially, there were concerns in markets and business over the effects of the Trump tariffs on the US economy. These have now given way to hopes over the prospects of deregulation, still lower interest rates, and tax cut extensions. This setup should benefit small and medium-sized companies, as should investment incentives, businesses reshoring, more lending by banks, and lower barriers to mergers and acquisitions.

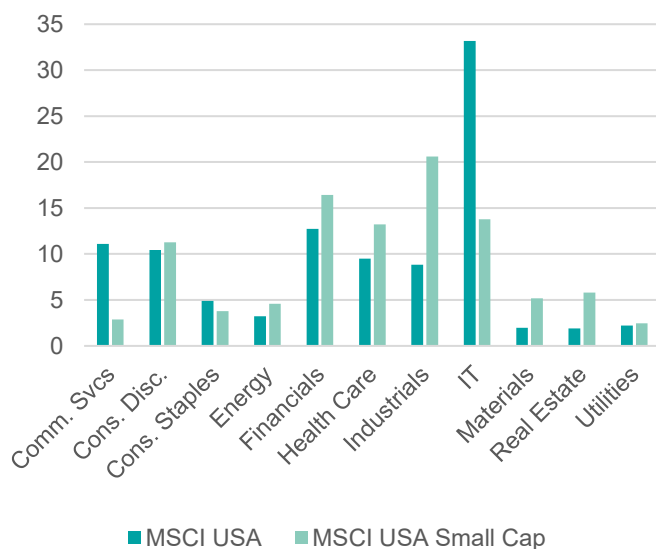
The small-cap equity market segment – and with it, small-cap indices – is usually more diversified than their large-cap counterparts. As a point in case, the MSCI USA Small Cap index covers more than 1,500 companies compared to only around 550 in the broad MSCI USA index. US small-cap indices tend to have a more balanced allocation to business sectors. Thus, the exposure to the technology sector, where we have seen a growing concentration of large and mega-cap companies in recent years (see Exhibit 1), is much more limited.

The heavy presence of the top 10 in large-cap indices reflects the impressive performance of the Magnificent 7 in recent years. Exhibit 2 shows that the top 10 accounts for around 40% of the MSCI USA index, where in the small-cap index, their cumulative weight is only around 4%.

With such a sizeable weight, the largest companies have been the main performance drivers of US large-cap indices: the top 10 contributed 50-60% to index returns in 2024 and 2025. In comparison, the top 10 contribution to the performance of the MSCI USA Small Cap index was only around 15% in 2025.

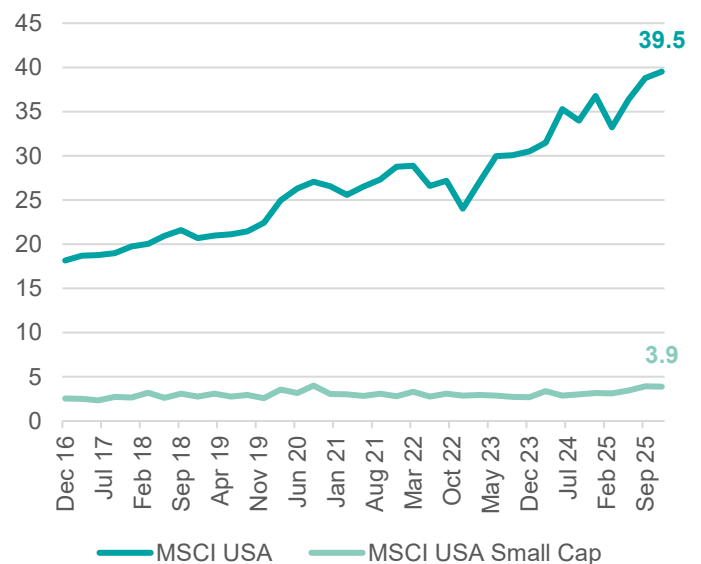
US Small cap index breakdown is more balanced

GICS level 1 sector breakdown, % of market value
Exhibit 1



Mag 7 dominate in US large-cap indices

Top 10 weight since December 2016 (quarterly, in %)
Exhibit 2



Source: BNP Paribas Asset Management, MSCI, Bloomberg as of 31/01/2026. Past performances are not indicative of current or future performance.

How index construction can shape small-cap passive exposure

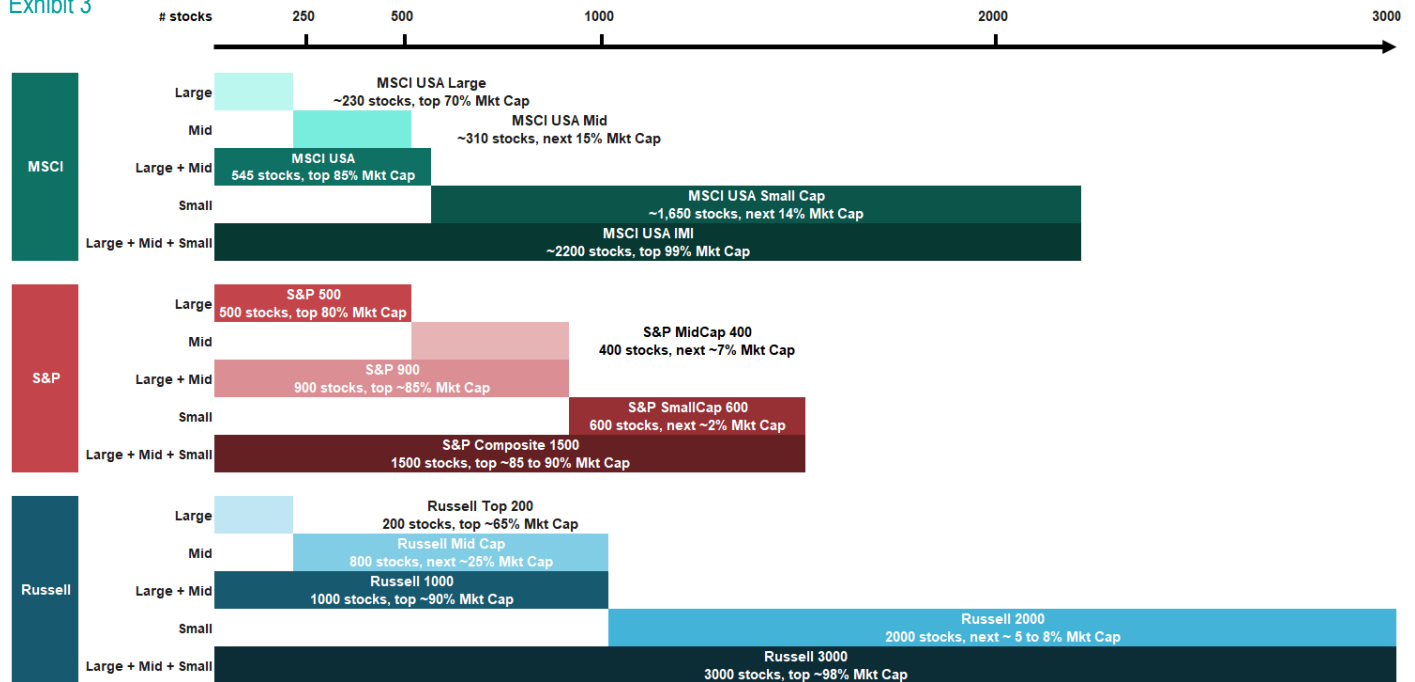
When looking at passive exposures to US small-cap stocks, it is important to understand the exact definition of the investment segment.

Exhibit 3 gives the definitions of the main index providers – it illustrates that the stocks selected can vary significantly. The difference in definition is also true for large and mid-cap indices, but as those indices nowadays tend to be concentrated in the mega caps, the impact is not as significant.

As an example, the overlap between the MSCI USA and the S&P 500 is more than 95% in terms of market value; it is a still high 89% for the MSCI USA Large Cap and the S&P 500. However, the overlap is only 25% between the MSCI and S&P small-cap indices, or 45% for the MSCI and FTSE Russell ones.

Methodology varies from one index provider to another

Exhibit 3



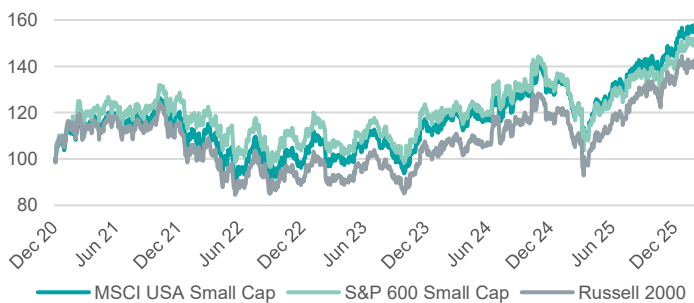
Despite showing similar behaviours, the performance of indices can diverge significantly as illustrated in Table 1 and Exhibit 4. For example, in the last 12 months the MSCI and Russell indices had comparable returns (roughly 23%), while the S&P index returned only around 17%.

The limited overlap and the differences in performance lead to a higher tracking error of small-cap indices compared to traditional large and mid-cap US equity benchmarks. This shows the importance of looking carefully at the definition of the universe when choosing a small-cap index.

Not all US small-cap indices perform identically

NTR historical performance of the different indices

Exhibit 4



— MSCI USA Small Cap — S&P 600 Small Cap — Russell 2000

Source: BNP Paribas Asset Management, MSCI, FTSE Russell, S&P indices, Bloomberg as of 27/02/2026. Past performances are not indicative of current or future performance.

Different composition leads to different performance

NTR performance in USD

Table 1

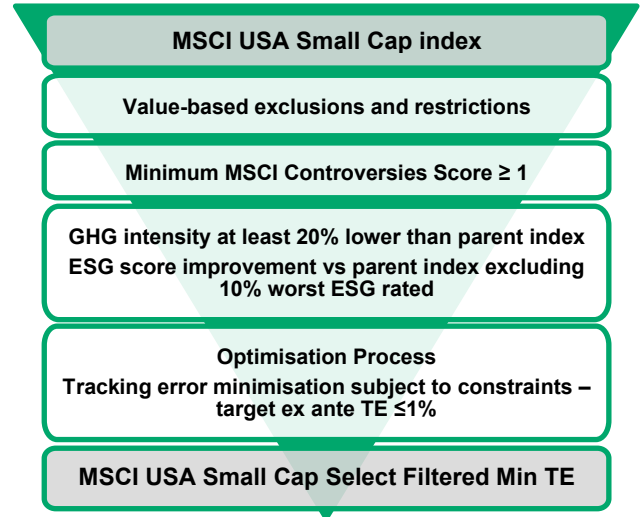
	MSCI USA Small Cap	S&P 600 Small Cap	Russell 2000
1Y perf	22.7%	17.3%	22.9%
3Y perf	46.6%	31.3%	43.1%
5Y perf	41.3%	30.9%	25.5%
1Y vol	18.4%	19.2%	19.3%
3Y vol	18.8%	19.4%	20.2%
1Y TE with MSCI Index	-	4.3%	3.0%

Embedding ESG considerations in your US small-cap exposure

Above, we discussed the merits of considering a US small-cap passive exposure as well as the importance of the universe definition across index providers. One additional consideration is the integration of environmental, social and governance factors. Indeed – just as with large-cap indices – ESG integration can be done in various ways in a US small-cap universe; it can also influence performance depending on how it is implemented.

The MSCI Select Filtered min TE methodology embeds ESG considerations in three main aspects*:

- **Value-based exclusions and restrictions:** companies involved in any of the below businesses are excluded – fossil fuel extraction thermal coal power, controversial weapons, tobacco production*
- **ESG score improvement:** the weighted average ESG score of the MSCI Select Filtered Min TE index is at least equal to the ESG score of the parent index after removal of the 10% worst ESG rated companies
- **Carbon intensity reduction:** greenhouse gas intensity is at least 20% lower than that of the parent index (including scope 1+2+3 GHG emissions).



The weights of the index constituents are determined using an optimisation process that aims at minimising the ex-ante tracking error against the parent index. This process embeds constraints including the carbon intensity and ESG score improvements mentioned above, but also criteria for the maximum deviations from the parent index at a sector, country and issuer level to make the ESG index as representative as possible versus mainstream small-cap exposures.

In the case of US small-cap exposure, embedding ESG considerations leaves 1,411 out of 1,628 constituents of the parent index in the MSCI Select Filtered Min TE universe. Incorporating these factors raises the industry-adjusted ESG score from 5.7 to 6.0, while the carbon intensity of the index falls from 519 tCO₂e/\$M EVIC* to 422. The effect on the tracking error is limited: 0.55% for one-year ex-post weekly returns and 0.50% on an ex-ante basis.

Despite better ESG metrics, the performance differences versus the mainstream index are minimal, and the volatility is almost identical (See Table 2). The MSCI USA Small Cap Select Filtered Min TE index appears to offer a similar portfolio profile compared to the parent index in terms of performance and breakdown with a contained tracking error.

Significant ESG improvement with limited performance deviations

Table 2

	MSCI USA Small Cap	MSCI USA Small Cap Select Filtered Min TE
Metrics		
# stocks	1,628	1,411
ESG score*	5.7	6.0
Carbon intensity*	519	422
Ex-ante TE	-	0.50%
Historical performances		
Perf 1Y	22.7%	22.9%
Perf 3Y	46.6%	46.0%
Vol 1Y	18.4%	18.6%
1Y TE	-	0.55%

Indicators such as the ESG score and carbon intensity can be improved on top of excluding controversial businesses and severe controversies (in line with UN Global Compact principles). We can conclude that the MSCI USA Small Cap Select Filtered Min TE index is an additional tool to integrate ESG considerations into passive portfolios, while maintaining similar features compared to mainstream exposures.

Source: BNP Paribas Asset Management, Bloomberg, MSCI as of 27/02/2026 (except on ESG and carbon related metrics, as of 30/01/2026). Past performances are not indicative of current or future performance.

*For detailed index rules, please refer to the MSCI methodology document on www.msci.com ** MSCI Industry adjusted ESG score, Weighted average scope 1, 2 and 3 carbon emissions intensity normalised by enterprise value including cash (unit: tons of CO₂/ \$ million enterprise value)

GLOSSARY

ETF	Exchange Traded Fund	TE	Tracking error
ESG	Environmental, Social and Governance	GHG	Greenhouse gas
AUM	Asset under management	SRI	Socially Responsible Investment
YTD	Year-to-date		

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