



## All In Favor. . . Say 'AI'!

---

 [westwoodgroup.com/design-matters/all-in-favor-say-ai](https://westwoodgroup.com/design-matters/all-in-favor-say-ai)

Recent articles highlight that the anticipated IPO of Space Exploration Technologies Corp., or SpaceX, is becoming closer to a reality as the company was hosting analysts and potential book runners last week. The company's valuation is now somewhere in the orbit of \$1.75 trillion, making the size of the IPO now being targeted as approximately \$85 billion, which would not only make SpaceX the largest IPO ever but also larger than the past three biggest IPOs to date: Saudi Aramco (~\$29.4 billion), Alibaba Group (~\$25 billion) and SoftBank Corp. (~\$23.5 billion).

Reuters reports that SpaceX plans to adopt a dual-class share structure. Under this setup, Class B shares would carry 10 votes each — consolidating control among Elon Musk and a small group of insiders — while the Class A shares sold to public investors would have one vote per share. The filing excerpts also indicate provisions that may limit shareholders' influence regarding board elections and constrain certain legal actions, including requiring disputes to go through arbitration and restricting the venues where claims can be filed.

Companies going public but not offering public investors voting control has been a source of friction for issuers, asset owners, governance advocates and index providers. Examples of recent issuance with uneven voting share structures were Snap in 2017, where the company IPO'd shares that had zero voting rights. Lyft and Uber offered dual-share classes where company insiders retained significant control, and Alphabet magnified this trend to three share classes (two public and one private) since 2014.

Listing authorities, exchanges and regulators have struggled with rules that often conflict between protecting the public's interests and the commercial competition to attract listings and the revenue from trading in the secondary markets. Historically, the presumed standard would be "1 share = 1 vote" and purchasers of the common equity shares would be able to influence company direction and decision via shareholder consensus. Governance and stewardship defenders depend on voting rights to provide

a layer of consumer advocacy over public companies. Traditional activist investors have a much more difficult time exerting pressure when they own share classes with no or diminished voting rights.

The Hong Kong exchange held tough on only allowing listings with equal voting rights but had to change their rules to not jeopardize losing out on the coveted Alibaba IPO. The UK listing authority also used to enforce equal voting rights as a requirement for listing but flexed to keep up with the lucrative trading and market data business that listings provide. The LSE now allows dual-class shares, but enhanced voting rights “must” expire after 10 years. Time will tell if this rule gets enforced or amended.

As much as the inequality of these voting share classes is a challenge for the exchanges, it’s magnified for the public investor; both via direct stock ownership and through indirect ownership via funds that track indexes.

Index providers have also had to re-evaluate their methodologies for how they treat public equities with multiple share classes. Eligibility rules that are strict and don’t allow multiple share classes risk missing out on major segments of the potential investable universe. Including all available share classes can result in concentration to a particular issuer and distort the weighting at the stock, sector and country level. Over the years, index providers have had to decide between keeping, breaking or bending their rules.

Since 2017, S&P Dow Jones deemed companies with multiple share classes ineligible for inclusion in the S&P 1500 universe but softened that stance by announcing, “effective April 17, 2023, all companies with multiple share class structures will be considered eligible candidates for addition to the S&P Composite 1500 and its component indices provided they meet all other eligibility criteria.”

MSCI Global Investable Market Index (GIMI) methodology allows multiple share classes to be eligible for inclusion but then adjusts the weighting based on the free float using an adjustment factor. Since the super/founder shares, generally those with empowered voting rights, are not available to the investing public, the index weight will be adjusted (down) accordingly.

FTSE Russell approaches it a bit differently, applying a minimum percentage of available voting rights to be eligible. Per the Russell methodology, “companies are required to have 5% or greater of the company’s voting rights (aggregated across all of its equity securities, including, where identifiable, those that are not listed or trading) in the hands of unrestricted shareholders or they will be deemed ineligible for index inclusion.”

The likelihood of some very sizeable IPOs happening soon is growing, and the valuations of the companies are unprecedented. In addition to SpaceX at ~\$1.75 trillion, OpenAI is rumored to be worth ~\$800 billion and Anthropic at ~\$300 billion. Should these companies choose to list without voting rights or list multiple share classes with uneven voting, they could be at risk of inclusion in some of the flagship indexes and the funds tracking them.

Given the size of the valuations and potential market capitalizations of these anticipated IPOs, perhaps the index providers should hold a vote on what companies get added.

Knowledge of the methodology of the underlying index is vital to understanding what exposures your index fund is providing. Not all indexes are the same and understanding how they are constructed can make a big difference in the investments you choose. The MIS team at Westwood Group believes that indexes are not all created equal, and index selection and design is an active decision. If you would like to discuss the nuances of indexing and explore designing a custom index that helps solve for your unique goals and outcomes, please reach out; we'd love to help provide a solution.

If you have questions or want help creating an investment strategy that fits your needs, we're here to help.

## **Author**

---

The information contained herein represents the views of Westwood Management at a specific point in time and is based on information believed to be reliable. No representation or warranty is made concerning the accuracy or completeness of any data compiled herein. Any statements non-factual in nature constitute only current opinion, which is subject to change. Any statements concerning financial market trends are based on current market conditions, which will fluctuate. Past performance is not indicative of future results. All information provided herein is for informational purposes only and is not intended to be, and should not be interpreted as, an offer, solicitation, or recommendation to buy or sell or otherwise invest in any of the securities/sectors/countries that may be mentioned.