Are Your Indexes Keeping Up with Mega-Cap IPOs?

Exploring how trillion-dollar market debuts are challenging traditional rules — and why investors must rethink benchmark alignment

Perspective from Gallagher's Investments practice

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Mega-Cap IPOs and Index Construction

Introduction

Investors are understandably enthused about the initial public offerings (IPOs) of SpaceX, OpenAI, and Anthropic, which provide an opportunity to gain a direct stake in companies at the forefront of artificial intelligence development. SpaceX went public on June 12, while OpenAI and Anthropic recently confidentially filed with the SEC for IPOs expected to occur later this year.

What's particularly notable about these public offerings is their size: SpaceX reached a market capitalization[1] of more than $2 trillion on its first trading day, while OpenAI and Anthropic may each achieve a $1 trillion public market valuation, based on their recent private market valuations. As such, as they gain admission into large cap market indexes, these IPOs will play a significant role in the US equity markets and market indices commonly used as performance benchmarks by investment managers.

Historically, companies rarely launched IPOs as large cap companies; rather, newly public companies were typically smaller, so their market impact was muted. Index providers had rules in place to bring these stocks into the indexes gradually. But as companies are now waiting longer to come to the public markets, in some cases their valuations are higher at the time they do so.

[1]The market capitalization of a stock equals its share price multiplied by the number of shares outstanding

Index Providers' Policies on IPOs

Index providers do not make changes to their policies in a vacuum. They consult with practitioners such as index managers, ETF issuers, and others to guide their decisions on when a stock should be included in an index. A well-designed index must be representative of the market, investable, and transparent. The changing nature of the companies preparing for an IPO, however, has forced the major index providers — including S&P, FTSE Russell, MSCI, and NASDAQ — to reconsider their methodologies, and they have adopted distinct approaches in dealing with the latest wave of mega-cap IPOs.

Of the four index providers, two chose to maintain their existing rules while two decided to implement faster entry timelines. One of the former was S&P, which considered but ultimately rejected making changes to its methodology. S&P requires companies to trade in the public markets for at least 12 months and meet certain profitability metrics (it is the only index provider with a profitability requirement). For example, it took ten years for Tesla to gain admission into the S&P 500 after its IPO. Another requirement is that companies must have a free float of at least 10% to be considered for inclusion,[2] which can pose a challenge for certain IPOs where much equity remains privately owned and restricted. Given these conditions, it is unlikely that the S&P 500 will include SpaceX or these other mega-cap IPOs anytime soon.

MSCI also elected to keep its existing rules in place, which allow companies to enter an index after just ten trading days. While it does not have a minimum requirement for free float, a stock's weight in an MSCI index is determined by its investable weight, or its free float percentage multiplied by its market capitalization.

[2]Free float represents the portion of a company's shares that are publicly traded and are not restricted or closely-held by company insiders.

FTSE Russell, on the other hand, took a different approach than S&P and MSCI. After much deliberation, it amended its index inclusion rules. FTSE Russell now permits faster entry into its indices, as soon as five days after a company goes public. This rule change applies to any company whose free float exceeds the low end of the Russell Top 500 index. Similar to MSCI and S&P, FTSE Russell weights its indices based on a company's free float, not its overall market capitalization. That means SpaceX may enter the Russell 1000 Index at ~0.11%, not a huge position. Over the 12 months following the IPO, though, more shares will become available for trading (i.e., increasing the free float), and SpaceX's weight in the index will likely increase.

One important wrinkle with respect to the FTSE Russell indices is that SpaceX may initially enter the Russell 1000 Value Index. When classifying stocks as Value or Growth, FTSE Russell typically relies upon publicly available company-level fundamentals. As a new public entity, SpaceX will not be able to provide this information, so FTSE Russell defaults to the average style characteristics of the company's sub-sector, in this case telecommunications, which is demonstrating strong value characteristics at this time. That said, FTSE Russell has the authority to adjust a company's classification at its discretion.

Finally, NASDAQ also modified its methodology for its NASDAQ 100 index. NASDAQ now requires companies to trade publicly for 15 days (down from three calendar months). The NASDAQ 100 index also considers a company's free float, but unlike its competitors NASDAQ adjusts a company's free float by a factor of three if that free float is less than 20% of a company's market capitalization. In the SpaceX example, its 4% free float thus becomes a 12% adjusted free float. So, these mega-cap IPOs will likely have much larger initial representation in the NASDAQ 100 than the other large cap indices.

Summary

As these mega-cap companies go through the IPO process and enter different market benchmarks, investors will need to understand these nuances of index construction. Passive index investors should determine if their index still reflects their investment beliefs. Is the selected index giving you the exposure that you desire? For active investors, your large cap managers will have to account for these stocks, and their performance will be influenced by their allocation (or lack thereof) to these companies. Just as the "Magnificent Seven" have been a dominant topic these late few years, the introduction of SpaceX, OpenAI, and Anthropic will likely produce a new narrative. The differences between the major US equity indices are increasing, and it's imperative that investors understand these details.

Summary of Index Provider Policies:

Index Provider	Modified policies?	Entry Timing	Minimum Float	Weight Adjustment	Rebalance
S&P	No	12 months	10%	None	Quarterly
FTSE Russell	Yes	T+5 days for mega IPOs	Possibly waive 5% float for large IPOs	None	Semiannual
MSCI	No	T+10	None	None	Quarterly
NASDAQ	Yes	If full market cap ranks within top 40 names, T+15	None	If float<20%, weight = 3x free float%	Quarterly

Aligning Your Portfolio Strategy with the New IPO Landscape

Institutional investors should be aware of the growing differences in large cap indices in light of the changes prompted by AI-driven mega-cap IPOs. These differences include index inclusion timing, free float constraints, and methodology, which can significantly alter exposure from one index to another. Engaging an institutional investment consulting firm can help validate whether your portfolio aligns with your strategic objectives, identify exposure gaps, and optimize implementation across passive and active strategies.

For over 20 years, Gallagher's Investments practice has supported institutional clients across public and private markets of varying size and complexity through comprehensive Summary Investment Reviews, helping reduce fees, enhance diversification, and strengthen governance through disciplined processes, independent assessment, and informed decision-making. Contact us for a consultation today.