

# Morningstar Europe: Star Rating and Category Enhancements

## Timeline

- 5 and 10-year star ratings: Available now in Morningstar Direct, using current rating methodology.
- 3, 5 and 10-year ratings with new cost methodology: Available with release of Oct. 31 month-end data.
- Overall rating with new methodology: Available with release of Oct. 31 month-end data.
- New categories: Available with release of Oct. 31 month-end data.

In 2001, Morningstar launched its Pan-European Rating and Fund Categories methodologies to provide investors, advisors, and institutions with a systematic framework for evaluating funds across Europe. We regularly assess our methodology to ensure that it maintains a consistent, accurate reflection of our investment landscape.

Effective October 31, 2006, Morningstar Europe will debut enhancements to further refine our rating system and categories. These improvements reinforce the key principles behind the rating system, which remain unchanged: To assess funds within their relevant peer group; evaluate funds over a long-term horizon; and adjust a fund's past performance according to both risk and fund costs. Morningstar Risk-Adjusted Return (MRAR) will continue to be the basis of the star-rating calculation.

Below is a brief overview of Morningstar's key changes for our European rating and categories.

## Rating Enhancements

We will introduce 5-year and 10-year star ratings to complement our existing 3-year star rating. These ratings reflect Morningstar's commitment to long-term investing, and better illustrate a fund's full performance history.

The overall star rating, (the rating used in most Morningstar materials, and the one that is most frequently cited in the press), will be based on a weighted average of the 3-, 5-, and 10-year ratings, depending on the length of the fund's performance record. This should give investors a clearer, more stable picture of a fund's performance history. It also unites Morningstar Europe and Morningstar US on a single global standard for fund ratings. The calculation will be as follows (when funds have changed categories during the rating period, the weights may be modified to put more emphasis on the funds' records in their current categories):

## Performance Record

36 – 59 months

60 – 119 months

120 months or longer

## Overall (Weighted) Rating

Overall = 100% 3-year rating

Overall = 60% 5-year rating  
40% 3-year rating

Overall = 50% 10-year rating  
30% 5-year rating  
20% 3-year rating

Total returns used in calculating the risk-adjusted return used for the star rating will continue to be adjusted for front-end sales charges, but will also now be adjusted for deferred sales charges and redemption fees.

## Category Enhancements

The Morningstar system for categorising funds is based on three guiding principles:

**Proper Evaluation:** Every category should form a benchmark against which a manager's ability to add value relative to managers with similar styles can be meaningfully measured.

**Distinctive Profiles:** Every category should be composed of funds that, in aggregate, have a risk-return profile that is distinguishable from that of other categories.

**Investor Utility:** A category will be created only if it can help investors and their advisers more accurately assess a fund's risk-return profile against a relevant universe.

In keeping with these principles, we are enhancing our system of categorisation as follows:

- Eurozone equity categories will be split into individual EMU country categories.
- Fixed-income categories will be refined by increasing their granularity across types of fixed-interest securities and currency exposures.
- Absolute-return and target date categories will be added.
- The convertibles category will be split into US Dollar/Global Convertibles and Euro Convertibles.
- Several economic sector categories will be added and/or refined.

## Preliminary List of Categories to be Added Effective 31 October, 2006.

### Balanced

SEK Aggressive Balanced  
SEK Cautious Balanced

### Bond

Asia/Japan Convertible Bond  
Emerging Europe Bond  
Euro Convertible Bond  
Euro Global Bond - Hedged  
Euro Inflation-Linked Bond

Euro Long Bond

Global High Yield Bond

Non-Euro Inflation-Linked Bond

USD/Global Convertible Bond

### Equity

Austria Equity

Belgium Equity

Canada Equity

Emerging Europe ex Russia Equity

Eurozone Single Country Equity

Finland Equity

France Large Cap Equity

France Small/Mid Cap Equity

Germany Large Cap Equity

Germany Small/Mid Cap Equity

Italy Equity

Netherlands Equity

Russia Equity

Spain Equity

Switzerland Small/Mid Cap Equity

Gold Equity

### Other

Absolute Return

Target Date 2000-2014

Target Date 2015+