Morningstar® Style Indexes

Key Attributes
- Comprehensive and non-overlapping approach forms an integrated system
- Robust 10-factor style methodology leads to precise stock classifications
- Stability buffers to reduce portfolio turnover
- Building blocks for efficient portfolio construction

In 1992, Morningstar charted new territory in the investment world with the creation of the Morningstar Style Box™. It categorized stocks by their growth or value orientation and market capitalization and represented—at a glance—a map of asset allocation choices. In 2002, Morningstar enhanced its style methodology, which uses 10 factors to identify distinct growth and value attributes, creates a logical, integrated framework for investment research, portfolio assembly, and market monitoring.

Morningstar Style Index Family
The Morningstar Style Index family consists of 16 indexes that track the U.S. equity market by capitalization and investment style to create an integrated system. The indexes were built using a comprehensive and non-overlapping approach based on the methodology of Morningstar Style Box.

Index Eligibility
Index constituents are drawn from the available pool of liquid U.S. domiciled stocks that trade on one of the three major exchanges. The following security types are excluded: American Depository Receipts; bulletin board stocks; convertible notes, warrants and rights; and limited partnerships.

Liquidity Requirements
Securities that have more than 10 non-trading days in the prior quarter or that have average daily trading volume over the preceding six months that falls in the bottom quartile are excluded.

Constituent Weighting
Index constituents are weighted according to their free float of shares outstanding. The free float is defined as a company's outstanding shares adjusted for block ownership to reflect only shares available for investment. The types of block ownership that are considered during float adjustment are cross ownership, government ownership, private ownership, and restricted shares.

Stability Buffers
To help ensure that index turnover reflects significant events, stocks are reclassified in terms of style or capitalization only if they move sufficiently beyond the break point between styles (value-core or core-growth break points) or capitalization (large-mid or mid-small). The range in which a stock movement is permitted without impacting the classification is called the buffer zone. Short-term movements of stocks into or within buffer zones do not result in index turnover.

Rebalancing & Reconstitution
Morningstar rebalances constituent shares and weights of its sector indexes quarterly in March, June, September, and December. Immediate rebalancing occurs if two constituents merge or a company's free-float changes by 10% or more. The indexes are reconstituted (stocks are added or removed from the indexes) twice annually in June and December.

Overview of the Style Index Family

Broad Market Index

US Market℠

Targets 97% market capitalization coverage

Capitalization Indexes

Large Cap℠   Mid Cap℠   Small Cap℠

Large Cap: 70% market capitalization
Mid Cap: 20% market capitalization
Small Cap: 7% market capitalization
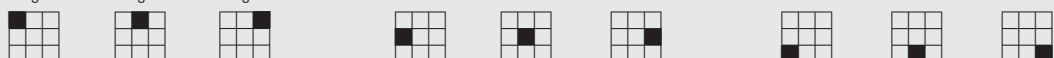
Composite Style Indexes

Value   Core   Growth

Value, Core, and Growth indexes are defined by 10 variables. Over 36-month rolling cycles, each index represents 1/3 of the overall market.

Style Indexes

Large Value℠   Large Core℠   Large Growth℠   Mid Value℠   Mid Core℠   Mid Growth℠   Small Value℠   Small Core℠   Small Growth℠
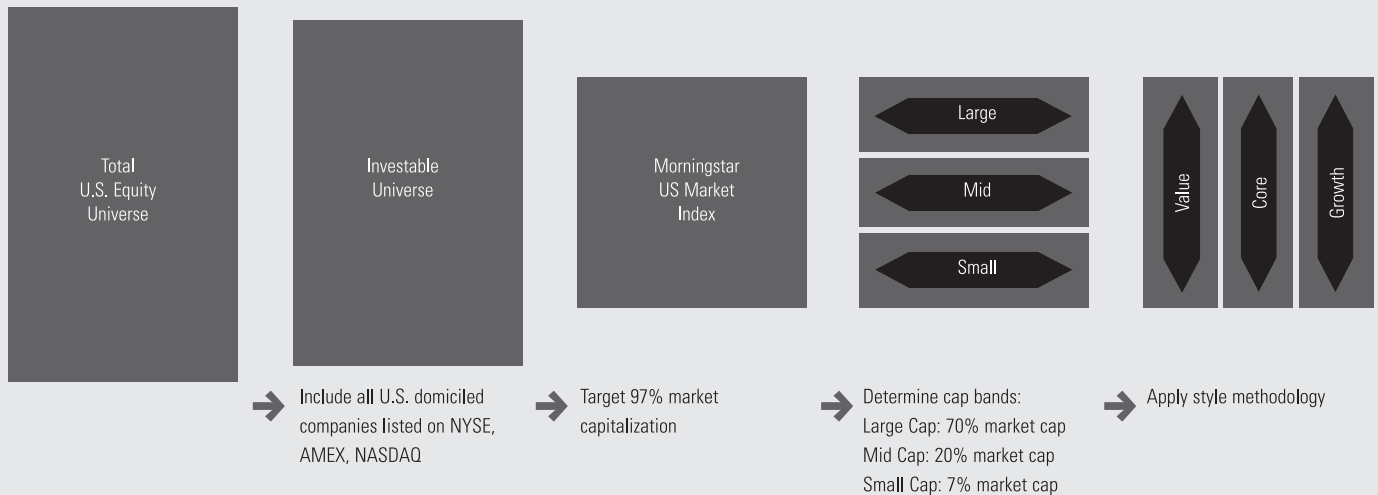
The nine segments of the well-known Style Box are specified by style and market capitalization.

Morningstar Index Construction Process

The index construction begins by defining the "investable portion" of the U.S. equity market. Next, liquidity screens are applied to create the Morningstar® US Market℠ Index, which targets 97% of the total capitalization of the U.S. market. The Morningstar US Market Index is divided into three market cap indexes by defining each as a percentage of the market capitalization of the investable universe.

Total U.S. Equity Universe

Investable Universe

Morningstar US Market Index

Large

Mid

Small

Value   Core   Growth

Include all U.S. domiciled companies listed on NYSE, AMEX, NASDAQ

Target 97% market capitalization

Determine cap bands:
Large Cap: 70% market cap
Mid Cap: 20% market cap
Small Cap: 7% market cap

Apply style methodology

Determining a Stock's Style

1. Determine a Value Score

Factors		Weight %
Forward-Looking	Price-to-Projected Earnings	50.0
Historical:	Price-to-Book	12.5
	Price-to-Sales	12.5
	Price-to-Cash Flow	12.5
	Dividend Yield	12.5

2. Determine a Growth Score

Factors		Weight %
Forward-Looking	Long-Term Projected Earnings Growth	50.0
Historical:	Earnings Growth	12.5
	Sales Growth	12.5
	Cash Flow Growth	12.5
	Book Value Growth	12.5

3. Determine a Style Score

Subtract the value score from the growth score.

Growth Score	0 to 100
Value Score	0 to 100
Style Score	−100 to 100

−100 Value | Core | Growth +100
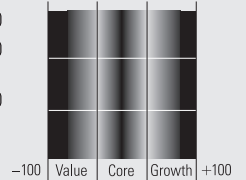
Determining a Stock's Style

Within each capitalization class, index constituents are assigned to one and only one of three style orientations—value, growth, or core—based on the stock's overall style score.

A stock's style score is determined by separately measuring a stock's value and growth characteristics using related but distinct historical and forward-looking variables, each accounting for one-half of a stock's style score. After calculating value and growth scores, they are compared to determine whether value or growth characteristics dominate. If the value-growth scores are not sufficiently different, the stock is designated core.

Breakpoints for value, core, and growth styles are set so that the average weight of each style over time represents approximately one-third of the investable universe within the capitalization class.

Contact Us

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