



Best MPF Scheme Award Methodology, Hong Kong

Morningstar Methodology Paper
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Morningstar Best MPF Scheme Award Methodology

The Morningstar Best MPF Scheme Award recognizes the MPF (mandatory provident fund) scheme which excels across the key qualitative and quantitative factors which we believe are important when selecting a retirement scheme. Our preferred schemes are those which deliver strong average risk-adjusted performance across its offerings, offer competitive fees, and have a keen consideration for product diversity, transparency and disclosure, and investor experience.

Only MPF schemes that are available to all individual employees are considered for this award. In addition, funds in the following categories are excluded from our assessment:

- ▶ Guaranteed Funds
- ▶ HKD Money Market
- ▶ Other Money Market
- ▶ Other Bond
- ▶ Other Equity
- ▶ Target Date
- ▶ DIS – Age 65 Plus Fund
- ▶ DIS – Core Accumulation Fund

Furthermore, we only consider categories with at least five distinct portfolios to ensure that we are making robust comparisons.

The award is annual, so we believe it is appropriate to emphasise the one-year average performance of funds within each scheme. However, as a long-term investment vehicle, we believe it is important for funds to have also delivered strong three- and five-year returns. Hence, only funds with at least five years of track record are considered in our award assessment.

Scoring System

The award is a combination of our quantitative, qualitative and fee assessment of an MPF scheme. The performance component accounts for 55% of the total score, whereas the qualitative and the fee components account for 25% and 20% of the total score, respectively. Our scoring system is as follows:

Performance Score (55% of total score)

Each fund in an MPF scheme is scored according to its risk-adjusted returns using the following method:

Return Score = 80% of Performance Score

One year: 30% of Performance score, based on 1-year return percentile rank in Morningstar Category

Three- and five-year: 50% of Performance score, of which

40% = 3-year return percentile rank in Morningstar Category

60% = 5-year return percentile rank in Morningstar Category

(Note: 3-year and 5-year scores are scaled to represent 40% and 60% of the long-term portion of the return score, respectively. The 3-year return score constitutes 20% of the performance score, and the 5-year return score constitutes 30% of the performance score.)

Risk Score = 20% of Performance Score

Of the risk score:

40% = 3-year Morningstar Risk percentile rank in Morningstar Category

60% = 5-year Morningstar Risk percentile rank in Morningstar Category

(Note: 3- and 5-year scores are scaled to represent 40% and 60% of the total risk score, respectively. The 3-year risk score constitutes 8% of the total score, and the five-year risk score constitutes 12% of the total score.)

A fund's performance score is the aggregate of its return and risk scores. The above scoring process is applied to each eligible fund in an MPF scheme, and an MPF scheme's overall performance score is the mean performance score of all of its eligible offerings. Each MPF scheme is then ranked in ascending order according to its overall performance score and assigned a percentile ranking. The scheme with the **highest** percentile ranking is the scheme which has delivered the best performance score.

Qualitative Score (25% of total score)

In addition to assessing each MPF scheme's average risk-adjusted performance, Morningstar's Hong Kong Manager Research team will review the qualitative aspects of each MPF scheme. There are three main areas of consideration:

- ▶ Product diversity – a scheme should offer a wide range of funds (e.g. multi-asset funds, passive investment options) that enables investors to construct a portfolio most suited to their needs.
- ▶ Transparency and disclosure – to help investors make an informed decision, a scheme provider should strive to provide full transparency to investors by disclosing information such as their fund's manager name, performance after fees, associated risks, etc. on a regular basis.
- ▶ Investor experience – investors should be able to access relevant information with ease. For that, a scheme provider should, among other things, provide a user-friendly website and a mobile app track and manage their investments, as well as provide regular investor education materials.

Each MPF scheme is scored according to the above criteria and ranked from the highest to the lowest. A percentile ranking is assigned accordingly; the higher the percentile ranking, the higher opinion we have on the qualitative aspects of the scheme.

Fee Score (20% of total score)

The final component of our scoring system constitutes an assessment of fees for each MPF scheme. Here, we have included funds in major asset classes that do not have a five-year track record, as we believe their fees remain relevant to investors. Each fund's net expense ratio is ranked within their respective Morningstar Categories. Decile rankings are assigned to funds in categories with 15 funds or more to better differentiate the wide range of fees observed. Quintiles are used for categories with less than 15 funds to take funds in the smaller categories into consideration.

Each fund is assigned a fee score using the above scoring process, and an MPF scheme's overall fee score is the mean fee score of all its eligible offerings. Each MPF scheme is then ranked from lowest to highest according to its overall fee score and assigned a percentile ranking. The scheme with the **highest** percentile ranking is the scheme which is the most competitively priced on average.

Award Selection

Based on the above weights, the effective weights of each component are as follows:

Performance Score (55%)	One-year returns	16.5%
	3-year returns	11%
	5-year returns	16.5%
	3-year Morningstar Risk	4.4%
	5-year Morningstar Risk	6.6%
Qualitative Score		25%
Fee Score		20%
		<hr/>
		100%

Upon the completion of the quantitative, qualitative and fee assessments, the MPF scheme with the highest total percentile ranking will receive the Morningstar Best MPF Scheme Award.