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2015 Market Classification Results

Greece to Be Reclassified as an Emerging Market

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The Morningstar Index Committee has confirmed that as part of its 2015 market classification review, Greece will be reclassified from developed markets to emerging markets, and Morocco from emerging markets to frontier markets effective at the June 2016 semiannual reconstitution. There are no changes in the market classification of the other countries/segments under review.

2015 Review Results

Greece

Greece will be reclassified as an emerging market as part of the August 2015 annual review.

Greece continues to experience political and economic instability, which poses significant risks to international institutional investors. Greece recently imposed capital controls and trade suspension, and ordered banks to close temporarily in June after the European Central Bank refused to increase emergency funding after bailout talks between Greece and foreign creditors broke down. As expected, Greece defaulted on a EUR 1.55 billion payment to the International Monetary Fund, resulting in speculation about its exit from European Union. Although it was able to make a EUR 6.8 billion payment to the ECB, the IMF, and the Bank of Greece, investors continue to face capital controls imposed in June that are gradually becoming more relaxed but are still far away from supporting the normal functioning of the market.

In light of the recent events and the uncertainty about its future, Greece no longer meets the requirement of a developed market and will therefore be reclassified as an emerging market at the June 2016 semiannual reconstitution.

Morocco

Morocco will be reclassified as a frontier market, because it fails to meet the minimum liquidity standards that currently prevail in emerging markets.

Coupled with degrading investment sentiment, liquidity has dropped significantly in the Moroccan equity market over the past few years. The government's announcement that it will permit short selling and offer incentive grants to encourage initial public offerings hasn't resulted in a boost in liquidity. Around 60% of the Moroccan equity universe fails liquidity screens, and the Morningstar Emerging Markets Index consists of only seven Moroccan companies, accounting for less than 20 basis points of weight in the index. All of these concerns highlight that Morocco no longer aligns with the emerging-market standards and hence will be reclassified as a frontier market.

South Korea

Morningstar Indexes will continue to classify South Korea as an emerging market because it fails to meet accessibility issues raised by institutional investors from other countries.

South Korea has consistently shown strong economic development over the last few years, and its market size and liquidity meet the criteria required for a developed market. However, the country has failed to address two significant issues that restrain foreign institutional investors from their customary trading practices. The Korean won still can't be obtained or converted outside the country and can be traded only during Korean business hours through local counterparties. The national ID system limits off-exchange transactions and in-kind transfers, constraining accessibility to the Korean market.

South Korea will remain on the August 2016 review list for potential reclassification as a developed market.

China A

Morningstar Indexes will continue to exclude China A shares from the Morningstar Emerging Markets Index.

There have been significant developments in Chinese markets over the last few years. The launch of the Qualified Foreign Institutional Investor, or QFII, and the Renminbi Qualified Foreign Institutional Investor, or RQFII, programs has improved the accessibility to the mainland A-share market considerably. However, investors still have concerns about the restrictions on cross-border capital flows. QFIIs can only buy China A shares worth CNY 13 billion each day, and the aggregate quota is limited to CNY 300 billion. The QFII quota has increased in recent years but still limits the exposure to this market for investors. In addition, individual ownership is limited to 10% of the shares of a listed company, and the A shares held under this program may not exceed 30% of a listed company.

Morningstar will continue to monitor the development in the China A market and will maintain it in the review list next year.

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Exhibit 1 2015 Morningstar Indexes Market Classification Results (⊕ Pass, ⊖ Fail, ● Restricted)

			Market Reclassification			Potential Addition to Emerging Markets Index
Criteria	Developed	Emerging	Greece	South Korea	Morocco	China A
World Bank GNI Per Capita Rating	High (3-yr cons.)	High/Middle	High	High	Lower Middle	Upper Middle Income
Degree of Economic Freedom Score	>50	>50	54	71.5	60.1	52.7
Credit Quality	—	—	Speculative	Investment	Speculative	Investment
Market Structure & Regulatory Environment						
Regulatory Environment	⊕	⊕	⊕	⊕	⊕	⊕
Equitable Treatment	⊕	—	⊕	⊕	⊕	⊖
Market Accessibility	⊕	⊕	⊖	●	⊕	⊖
Market Structure-Equity	⊕	⊕	⊕	⊕	⊖	⊕
Market Structure-FX	⊕	⊕	⊕	●	●	⊖
Trading Conditions						
Ease of Entering Market for Foreign Investors	⊕	⊕	⊕	⊕	⊕	⊖
Quality of Brokerage	⊕	⊕	⊕	⊕	⊕	⊕
Market Liquidity	⊕	⊕	⊖	⊕	⊖	⊕
Capital Flow (Inflow/Outflow)	⊕	⊕	⊖	⊕	⊕	⊖
Nominal Transaction Costs	⊕	⊕	⊕	⊕	⊕	⊕
Short Selling Allowed	⊕	—	⊕	⊕	⊖	⊖
Off-Exchange Transactions Allowed	⊕	—	●	●	⊖	⊖
Stock Lending and Margin Trading	⊕	—	●	⊕	●	⊖
Transparency	⊕	⊕	⊕	⊕	⊕	⊕
Taxes	⊕	—	—	—	—	—
Settlement						
Clearing and Settlement Cycle	⊕	⊕	T+3	T+2	T+3	T+0
Quality of Custodian Services	⊕	⊕	⊕	⊕	⊕	⊕
Delivery Free of Payment Facility Available	⊕	—	⊕	●	⊖	⊖
Availability of Omnibus Account Facilities	⊕	⊕	●	⊕	⊕	⊕
Market Capitalization	>$5 Billion	>$5 Billion	⊕	⊕	⊕	⊕
Ratio of Market Capitalization to GDP	Top 80%	Top 80%	⊕	⊕	⊕	⊕
Market Classification Results	—	—	Emerging	Unchanged	Frontier	Not Added

2016 Review List

As part of the August 2016 review, the Morningstar Index Committee will continue to monitor the following countries/market segments for potential reclassification.

China A Shares	Potential reclassification from stand-alone market to emerging market.
Pakistan	Potential reclassification from frontier market to emerging market.
Peru	Potential reclassification from emerging market to frontier market.
Saudi Arabia	Potential reclassification from stand-alone market to emerging market.
South Korea	Potential reclassification from emerging market to developed market.

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