

Morningstar Wide Moat Focus Index: 2023 Year in Review

Morningstar Equity Research

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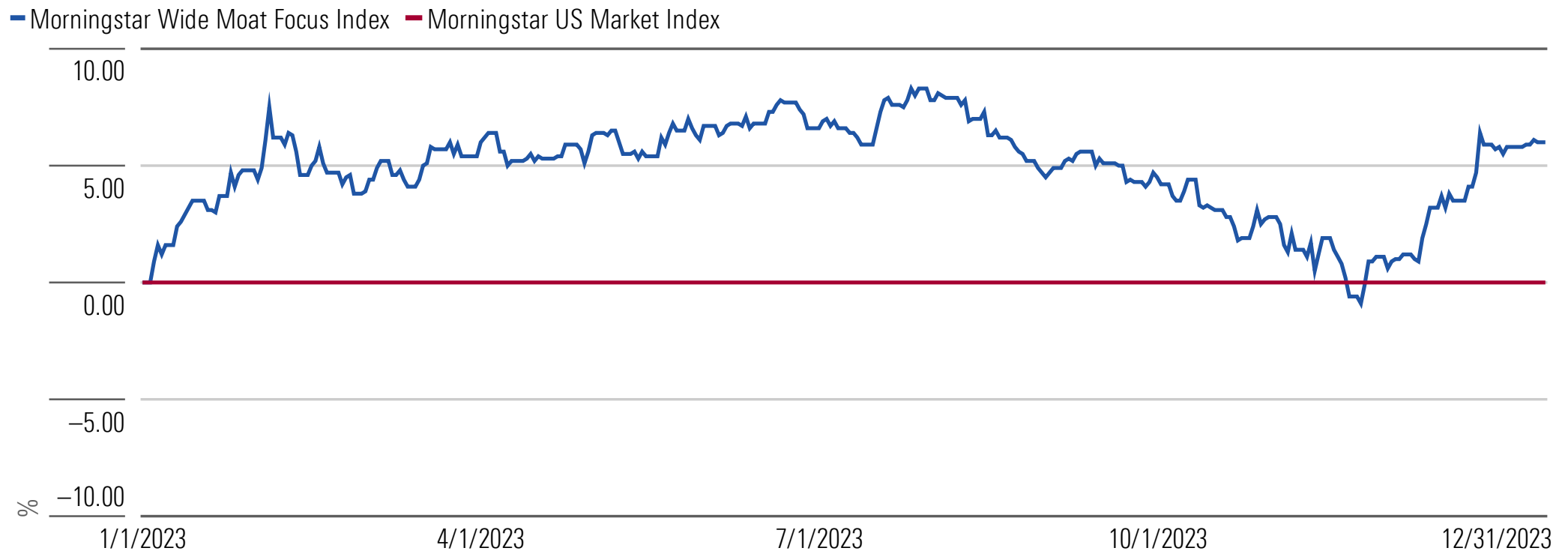
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Performance Review & Analysis

A Late-Year Resurgence Locked in Sizable Excess Returns

The Morningstar Wide Moat Focus Index delivered strong outperformance versus its benchmark through July-end, peaking at +834 basis points. These gains eroded over the next few months, with the Index trailing its benchmark by mid-November. This decline was catalyzed by an atypically high number of disappointing 3Q earnings releases across its holdings. However, favorable stock selection restored strong outperformance from late-November through year-end. The index outperformed its benchmark by +597 basis points on the full year.



Time Period: 1/1/2023 – 12/31/2023

Source: Morningstar Direct

Indexes are unmanaged and not available for direct investment

Strong 2023 Results Enhanced Long-Term Outperformance

The Morningstar Wide Moat Focus Index has now outperformed its benchmark over six of the last eight years. Annualized total returns since the index's February 2007 live inception date reached +327 basis points by year-end. This outperformance has been observed across both up markets and down markets. For example, since inception, the index held up better than its benchmark each year that the benchmark has declined (2008/2018/2022) but has then proceeded to outperform in each subsequent recovery year (2009/2019/2023).

Index Name	Trailing 1-Year	Trailing 3-Year	Trailing 5-Year	Trailing 10-Year	Live Inception
Morningstar Wide Moat Focus Index	32.41	12.84	17.53	13.48	12.68
Morningstar US Market Index	26.43	8.62	15.25	11.60	9.41
+/-	5.97	4.22	2.28	1.88	3.27

Index Name	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Morningstar Wide Moat Focus Index	-5.39	-19.58	46.93	8.57	6.61	24.50	31.46	9.68	-4.28	22.37	23.79	-0.74	35.65	15.09	24.81	-13.08	32.41
Morningstar US Market Index	2.47	-37.03	28.45	16.80	1.58	16.27	33.13	12.85	0.69	12.44	21.47	-5.05	31.22	20.90	25.78	-19.43	26.43
+/-	-7.85	17.46	18.48	-8.23	5.03	8.24	-1.68	-3.17	-4.97	9.93	2.32	4.31	4.43	-5.81	-0.98	6.35	5.97

Time Period: 2/14/2007 – 12/31/2023

Benchmark: Morningstar US Market Index

Source: Morningstar Direct

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Being Underweight the “Magnificent 7” Represented a Performance Headwind

All “Magnificent 7” companies soundly outperformed the broader US equity market in 2023. Given their massive market caps, this was the primary reason market cap-weighted U.S. indexes tended to outperform their equal-weighted counterparts. The “Magnificent 7” accounted for a 22.52% weighting in the broad-based Morningstar US Market Index but only a 8.95% weighting in the Morningstar Wide Moat Focus Index. They accounted for just over 50% of the benchmark’s total return in 2023 but only 26% of the index’s total return. Overall, this basket drove a -195 basis point active return for the index in 2023, as only Meta Platforms provided a tailwind for relative performance.

Company	Weight %			Total Return %	Contribution %		Active Return %
	Index	Benchmark	+/-		Index	Benchmark	
Apple Inc	-	6.22	-6.22	49.00	-	2.58	-1.21
Microsoft Corp	1.98	5.65	-3.67	58.19	1.23	2.83	-0.88
Alphabet Inc	2.59	3.17	-0.58	58.58	1.36	1.58	-0.14
Amazon.com Inc	1.94	2.60	-0.66	80.88	1.50	1.67	-0.08
NVIDIA Corp	0.40	2.12	-1.71	239.02	1.21	2.36	-0.85
Tesla Inc	-	1.42	-1.42	101.72	-	0.92	-0.67
Meta Platforms Inc	2.04	1.36	0.68	194.13	3.25	1.43	1.89
Total	8.95	22.52	-13.57		8.55	13.37	-1.95
				2023 Total Return %:	32.41	26.43	
				% of 2023 Total Return From "Magnificent 7":	26.38	50.59	

Time Period: 1/1/2023 – 12/31/2023

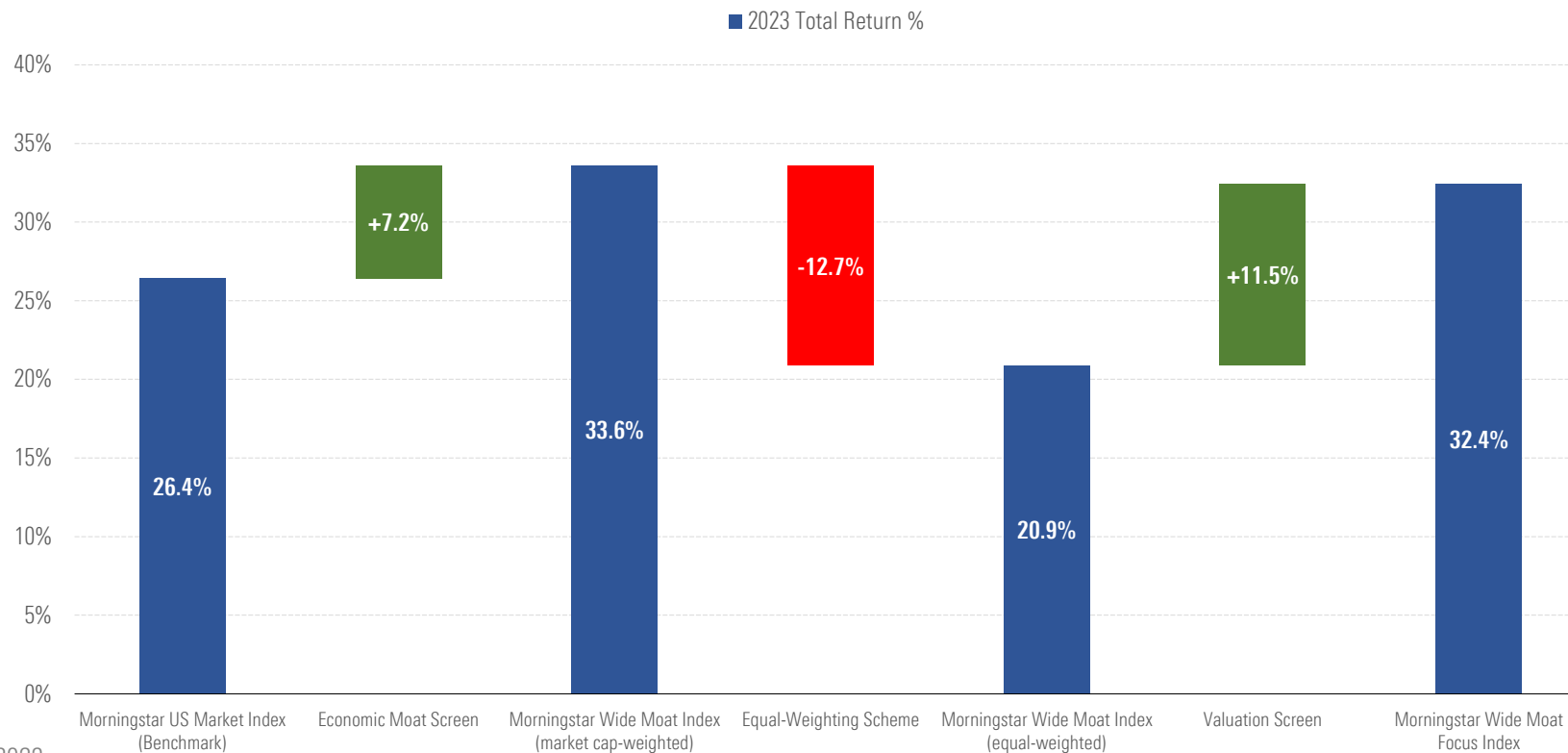
Benchmark: Morningstar US Market Index

Source: Morningstar Direct

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The Index Overcame a Stiff Performance Headwind From Its Equal-Weighting Approach

With the “Magnificent 7” stocks having driven a over half of the broad market’s total returns in 2023, equal-weighted indexes faced a pressing performance headwind. Indeed, the Morningstar Wide Moat Index, a market cap-weighted index of all U.S. wide moat-rated stocks, soundly outperformed its equal-weighted counterpart (as seen in the two middle blue bars below). However, for the Morningstar Wide Moat Focus Index, which screens for wide-moat U.S. stocks but adds a valuation screen, favorable stock selection allowed it to beat its benchmark by a wide margin.



Time Period: 1/1/2023 – 12/31/2023

Source: Morningstar Direct

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Both Sector Positioning and Stock Selection Proved Favorable

Stock selection within a sector, rather than relative sector positioning, has historically driven the lion's share of excess returns for the Morningstar Wide Moat Focus Index. In 2023, however, sector positioning had a more substantial positive impact. In particular, the index benefitted from holding no energy stocks, as the energy sector underperformed. Exposure to the technology sector is also noteworthy, as the index was overweight technology early in the year when the sector performed best but ended up significantly underweight by year-end as the sector's performance leveled out. Therefore, the index enjoyed a positive technology sector allocation effect despite being underweight an outperforming sector, on average.

Sector	Weight %			Total Return %		Contribution %		Performance Attribution		
	Index	Benchmark	+/-	Index	Benchmark	Index	Benchmark	Allocation Effect %	Selection Effect %	Excess Return %
Basic Materials	5.65	2.52	3.13	0.30	14.91	0.18	0.40	-0.32	-0.94	-1.26
Communication Services	9.58	7.71	1.87	62.25	54.60	5.47	3.65	0.70	0.77	1.47
Consumer Cyclical	9.60	10.84	-1.24	29.65	40.19	2.62	4.03	-0.11	-1.01	-1.11
Consumer Defensive	3.79	6.37	-2.59	-7.87	1.90	-0.27	0.14	0.79	-0.42	0.37
Energy	-	4.56	-4.56	-	-0.52	-	-0.03	1.42	0.00	1.42
Financial Services	15.48	12.81	2.67	24.90	16.18	5.39	2.24	0.46	1.87	2.33
Healthcare	15.22	13.52	1.70	9.13	2.24	1.32	0.34	0.12	0.65	0.76
Industrials	15.86	9.17	6.68	23.68	21.11	4.23	2.02	-0.38	0.48	0.10
Real Estate	-	3.05	-3.05	-	11.89	-	0.40	0.51	0.00	0.51
Technology	24.27	26.83	-2.56	61.33	58.48	14.72	13.47	0.91	0.90	1.81
Utilities	0.56	2.62	-2.05	-13.35	-7.05	-0.18	-0.22	0.75	-0.11	0.63
Total	100	100		33.49	26.45	33.49	26.45	4.85	2.19	7.04
								Reported Excess Return:		5.97

*** Reported returns for the index and benchmark were 32.41% and 26.43%, respectively, after accounting for residuals.

Time Period: 1/1/2023 – 12/31/2023

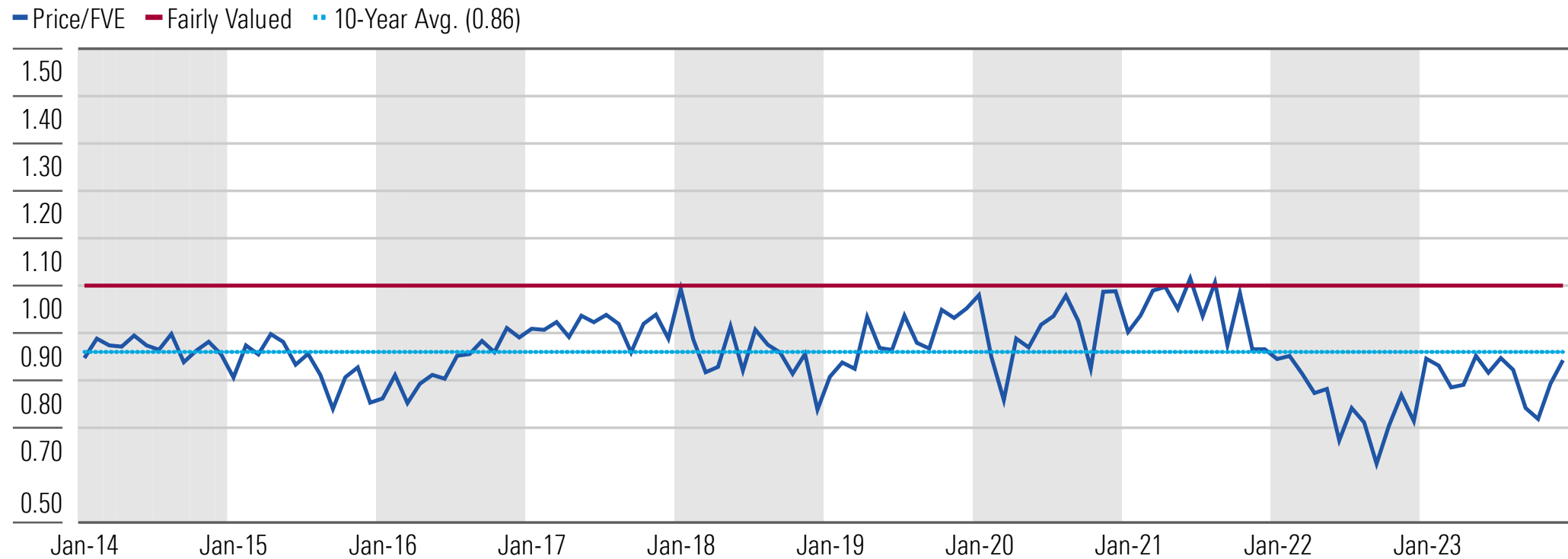
Benchmark: Morningstar US Market Index

Source: Morningstar Direct

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Despite Recent Outperformance, the Index Continues To Offer an Attractive Discount To Fair Value

Thanks to the Morningstar Wide Moat Focus Index’s rules-based reconstitution process, undervalued stocks are cycled in each quarter to replace holdings no longer trading at attractive valuations. As a result, the index has almost always operated at a discount to fair value, with fair value estimates determined by Morningstar equity analysts. Despite the index soundly outperforming its benchmark each of the last two years and despite the broad US equity market enjoying a 26.4% total return in 2023, the Morningstar Wide Moat Focus Index holdings still offered a healthy discount to fair value at 2023 year-end. Its 0.86 P/FVE ratio at year-end was in line with its 10-year historical average.



Time Period: 1/1/2014 – 12/31/2023

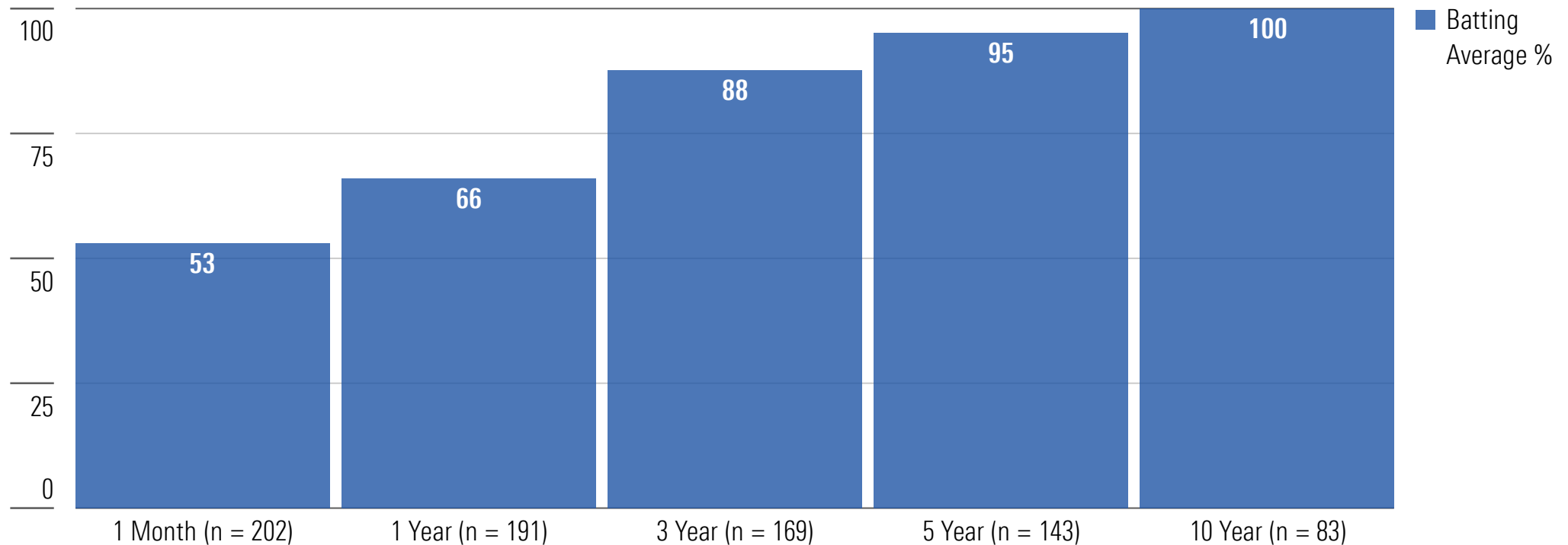
Methodology: Weighted avg. P/FVE via security-level weightings in portfolio

Source: Morningstar Direct

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The Index Has Enjoyed an Impressive Outperformance “Batting Average” Over Longer Holding Periods

Historically, the longer the holding period, the more consistent the outperformance for the Morningstar Wide Moat Focus Index. When considering monthly rolling time periods, the index has only outperformed its benchmark in 53% of its 202 months since inception. However, as the holding period extends, the index’s batting average steadily rises. It has outperformed 88% of the time over 3-year periods and 95% of the time over 5-year periods across large sample sizes. The index has outperformed its benchmark over all 83 of its 10-year holding periods since its launch.



Time Period: 3/1/2007 – 12/31/2023

Benchmark: Morningstar US Market Index

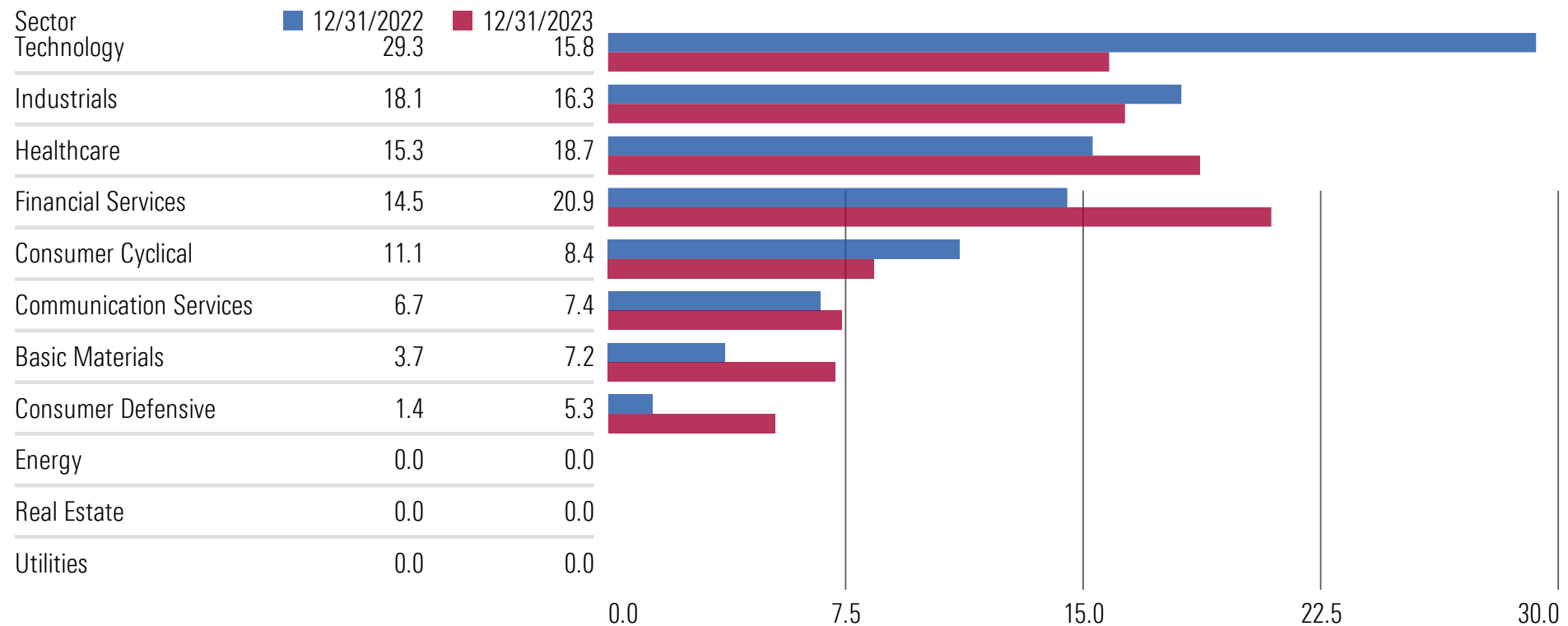
Source: Morningstar Direct

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Positioning & Characteristics

Sector Weightings Drifted Towards a More “Defensive” Positioning

The Morningstar Wide Moat Focus Index’s sector overweightings tend to drift wherever Morningstar equity analysts see the most attractive valuation opportunities on a stock-by-stock basis. Technology sector exposure declined significantly over the course of 2023 while exposure to the financial services, healthcare, basic materials and consumer defensive sectors increased. This represents a shift towards a “defensive” positioning, away from a more tech-heavy, “cyclical” positioning at the beginning of the year. The index is now more diversified as well, with no sector accounting for more than a 21% weighting or less than a 5% weighting (aside from energy, real estate, and utilities, which maintain a weighting of zero).



Time Period: 1/1/2023 – 12/31/2023

Source: Morningstar Direct

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The Index Migrated Towards a “Value” Style Bias and “Smaller” on the Market Cap Spectrum

Over the course of 2023, the Morningstar Wide Moat Focus Index was subject to a sizable shift, both in terms of its size and style orientations. With regard to style, the index started the year on the border between “growth” and “blend”, remaining there for the first half of the year. However, the June 2023 reconstitution catalyzed a shift towards a modest “value” bias at the expense of “growth”. Meanwhile with the growth-oriented “Magnificent 7” having performed well and, therefore, having grown to an even heftier combined weighting in the benchmark, the benchmark gradually migrated towards a more notable “growth” bias.

With regard to size, the index moved down the market cap spectrum. This was due, in part, to a decreasing exposure to the “Magnificent 7” over the course of the year but also to the increasingly attractive valuations of eligible mid-cap stocks relative to large- and mega-cap stocks. While it still operates in the large-cap band, the Morningstar Wide Moat Focus Index currently skews “smaller” than it has in recent years.

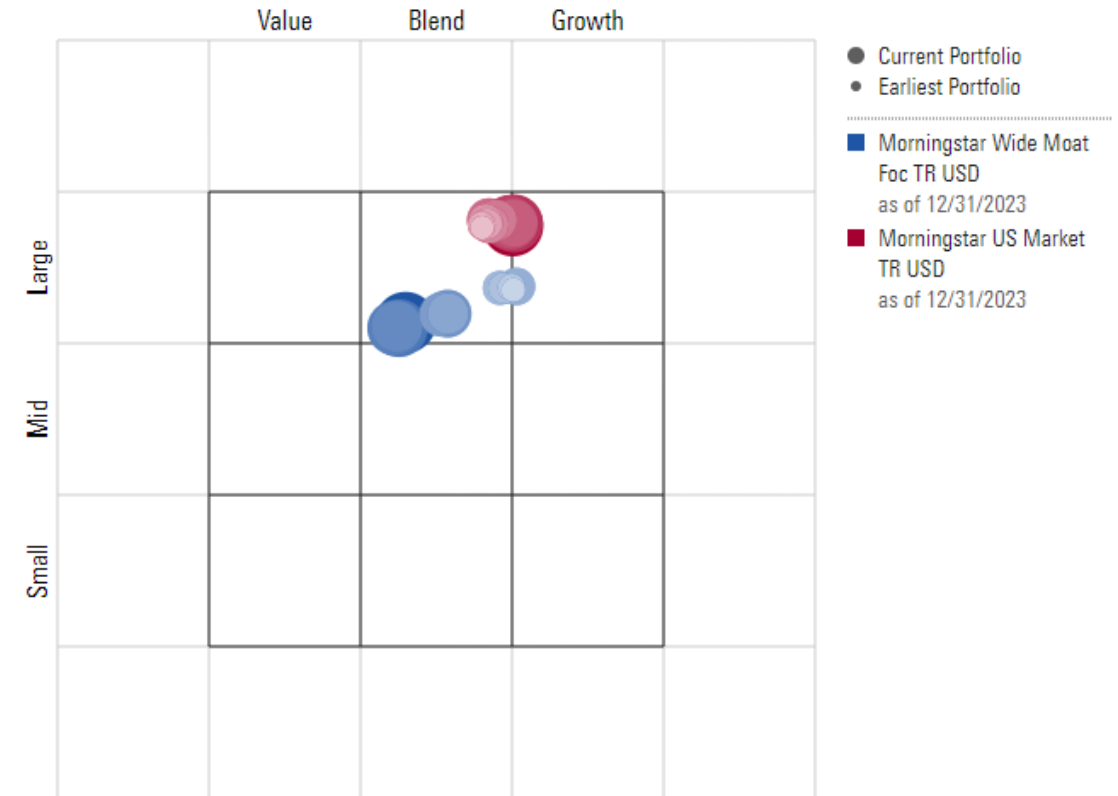
While these size and style shifts were more rapid than most historical shifts over a single calendar year, they are not unprecedented. Indeed, the index’s positioning can shift quickly when market conditions change. This versatility has helped the index outperform across a variety of market environments, as exhibited by an up capture of 109 and a down capture of 87 on a quarterly basis since inception.

Time Period: 1/1/2023 – 12/31/2023

Source: Morningstar Direct

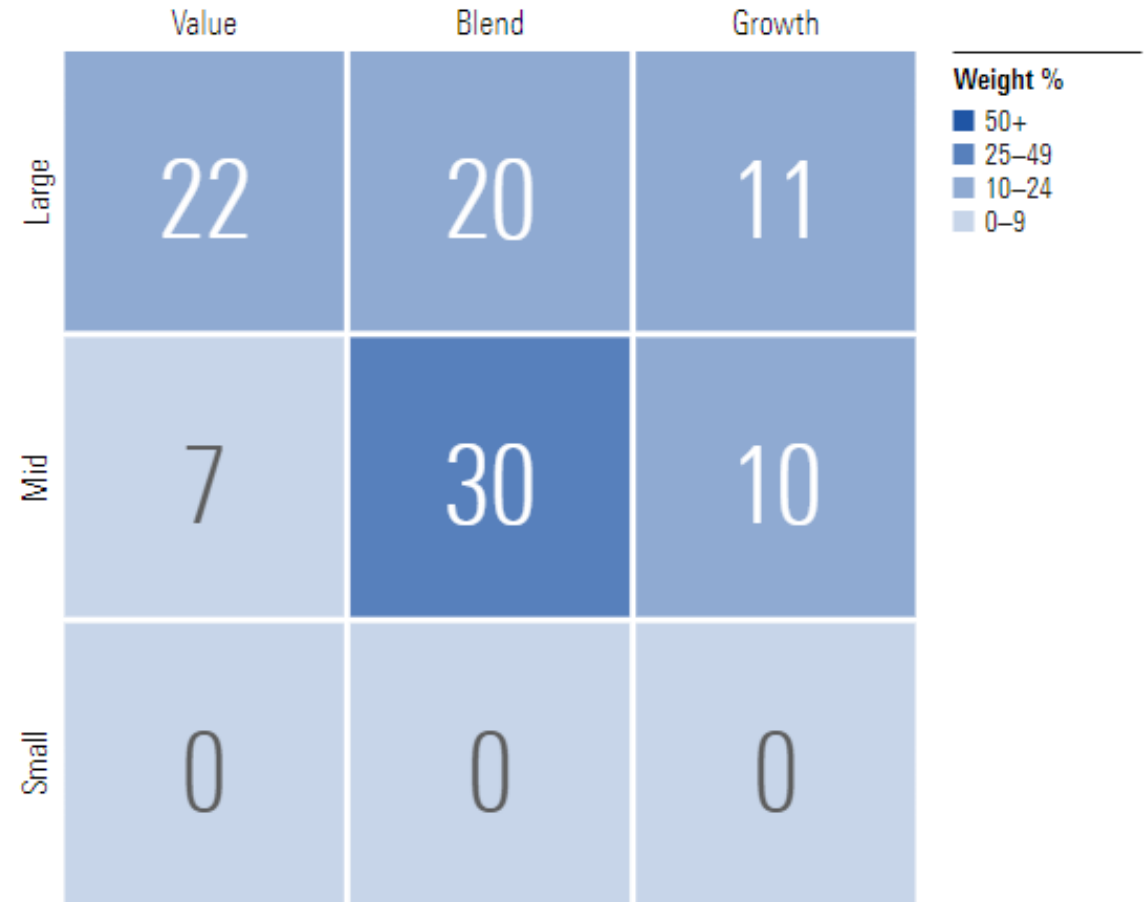
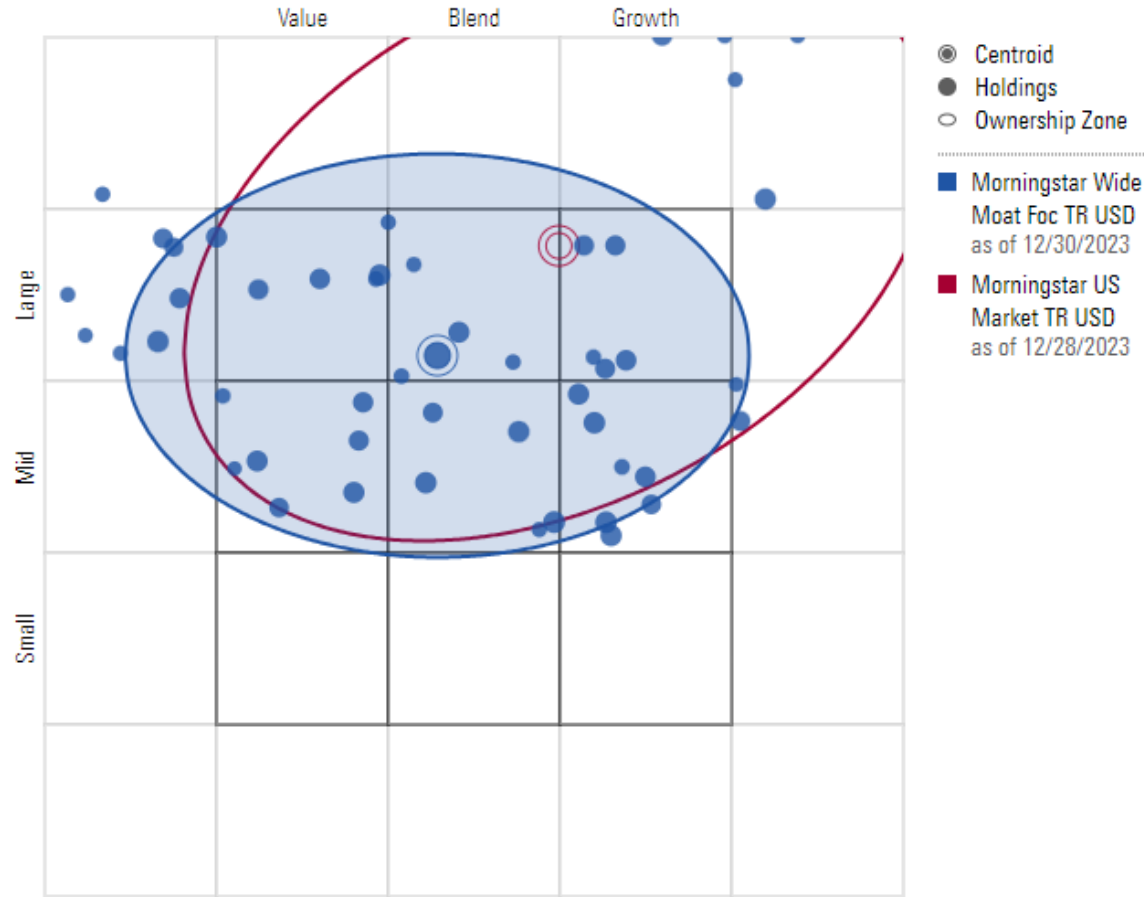
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2023 Style Box Positioning (Monthly)



Note: The larger and darker the bubble, the more recent the monthly data point.

Size & Style Composition



Data as of: 12/31/2023

Source: Morningstar Direct

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Holdings & Highlights

2023 Year-End Holdings

Name	Ticker	Sector	Weight %	Name	Ticker	Sector	Weight %
Allegion PLC	ALLE	Industrials	2.79	Comcast Corp	CMCSA	Communication Services	2.34
MarketAxess Holdings Inc	MKTX	Financial Services	2.74	Veeva Systems Inc	VEEV	Healthcare	2.32
Equifax Inc	EFX	Industrials	2.72	Corteva Inc	CTVA	Basic Materials	2.31
U.S. Bancorp	USB	Financial Services	2.72	TransUnion	TRU	Industrials	2.28
Teradyne Inc	TER	Technology	2.70	Campbell Soup Co	CPB	Consumer Defensive	2.25
Keysight Technologies Inc	KEYS	Technology	2.67	Pfizer Inc	PFE	Healthcare	2.15
Etsy Inc	ETSY	Consumer Cyclical	2.66	BlackRock Inc	BLK	Financial Services	1.36
Salesforce Inc	CRM	Technology	2.65	Microchip Technology Inc	MCHP	Technology	1.33
Charles Schwab Corp	SCHW	Financial Services	2.65	Waters Corp	WAT	Healthcare	1.33
Agilent Technologies Inc	A	Healthcare	2.63	Microsoft Corp	MSFT	Technology	1.32
Masco Corp	MAS	Industrials	2.62	Emerson Electric Co	EMR	Industrials	1.30
Intercontinental Exchange Inc	ICE	Financial Services	2.61	Bank of America Corp	BAC	Financial Services	1.29
Wells Fargo & Co	WFC	Financial Services	2.61	Bank of New York Mellon Corp	BK	Financial Services	1.28
International Flavors & Fragrances Inc	IFF	Basic Materials	2.59	Amazon.com Inc	AMZN	Consumer Cyclical	1.26
Tyler Technologies Inc	TYL	Technology	2.51	Roper Technologies Inc	ROP	Technology	1.26
Ecolab Inc	ECL	Basic Materials	2.50	Thermo Fisher Scientific Inc	TMO	Healthcare	1.26
RTX Corp	RTX	Industrials	2.46	Huntington Ingalls Industries Inc	HII	Industrials	1.25
Biogen Inc	BIIB	Healthcare	2.44	Honeywell International Inc	HON	Industrials	1.24
Alphabet Inc	GOOGL	Communication Services	2.43	3M Co	MMM	Industrials	1.23
Gilead Sciences Inc	GILD	Healthcare	2.42	Bristol-Myers Squibb Co	BMJ	Healthcare	1.20
Nike Inc	NKE	Consumer Cyclical	2.38	Berkshire Hathaway Inc	BRK.B	Financial Services	1.18
Zimmer Biomet Holdings Inc	ZBH	Healthcare	2.37	Altria Group Inc	MO	Consumer Defensive	1.14
Medtronic PLC	MDT	Healthcare	2.37	Fortinet Inc	FTNT	Technology	1.12
The Walt Disney Co	DIS	Communication Services	2.36	Kellanova Co	K	Consumer Defensive	1.06
The Estee Lauder Companies Inc	EL	Consumer Defensive	2.35				

Data as of: 12/31/2023

Source: Morningstar Direct

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Meta Platforms, Salesforce, and MarketAxess Stood Out As Strong Performers

In looking at top contributors to active returns for the Morningstar Wide Moat Focus Index in 2023, technology-oriented holdings dominate the list. Meta Platforms performed exceptionally well, delivering a 149% total return during its time as a holding. On the other side of the coin, underweight positions in Apple, Microsoft, Nvidia, and Tesla weighed on relative performance. Nvidia was a constituent entering the year but was removed after the March reconstitution as a period of strong performance pushed its stock price above our fair value estimate. Therefore, its average full-year weighting in the index was well below that of its benchmark as the stock delivered a 239% total return over the calendar year.

Company	Weight %			Total Return %		Contribution %		Active Return %
	Index	Benchmark	+/-	Index	Benchmark	Index	Benchmark	
Meta Platforms Inc	2.04	1.36	0.68	149.47	194.13	3.25	1.43	1.89
Salesforce Inc	2.75	0.49	2.26	98.46	98.46	2.14	0.35	1.32
MarketAxess Holdings Inc	1.27	0.03	1.24	58.45	6.11	1.33	0.00	1.00
MercadoLibre Inc	1.12	0.14	0.98	39.98	85.71	1.12	0.09	0.89
Lam Research Corp	1.68	0.19	1.48	50.52	88.61	1.26	0.14	0.88
Guidewire Software Inc	1.05	0.02	1.03	87.97	74.30	1.04	0.01	0.84
Adobe Inc	1.72	0.51	1.21	51.52	77.28	1.28	0.33	0.74
ServiceNow Inc	1.65	0.26	1.39	43.96	81.96	1.07	0.18	0.66
Charles Schwab Corp	1.00	0.23	0.76	22.42	-15.96	0.75	-0.06	0.58
Masco Corp	2.47	0.03	2.44	46.56	46.56	1.16	0.01	0.50

Company	Index	Benchmark	+/-	Benchmark	Benchmark	Index	Benchmark	Active Ret%
Tesla Inc	-	1.42	-1.42	-	101.72	-	0.92	-0.67
The Western Union Co	0.80	0.01	0.79	-11.19	-6.30	-0.35	0.00	-0.71
Kellanova Co	2.00	0.04	1.96	-7.59	-7.59	-0.16	0.00	-0.72
Zimmer Biomet Holdings Inc	2.37	0.07	2.30	-3.81	-3.81	-0.10	0.00	-0.80
NVIDIA Corp	0.40	2.11	-1.71	90.10	239.02	1.21	2.36	-0.85
Microsoft Corp	1.98	5.65	-3.67	58.19	58.19	1.23	2.83	-0.88
Biogen Inc	2.41	0.10	2.32	-6.55	-6.55	-0.18	-0.01	-0.90
International Flavors & Fragrances Inc	2.27	0.05	2.22	-19.48	-19.48	-0.41	-0.01	-1.16
Apple Inc	-	6.22	-6.22	-	49.00	-	2.58	-1.21
Etsy Inc	2.18	0.03	2.15	-32.33	-32.33	-0.77	-0.01	-1.51

Time Period: 1/1/2023 – 12/31/2023

Source: Morningstar Direct

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Top Active Return Contributors: Meta Platforms (META)



Time Period: 1/1/2021 – 12/31/2023

Source: Morningstar Direct

Indexes are unmanaged and not available for direct investment

Top Active Return Contributors: Salesforce (CRM)

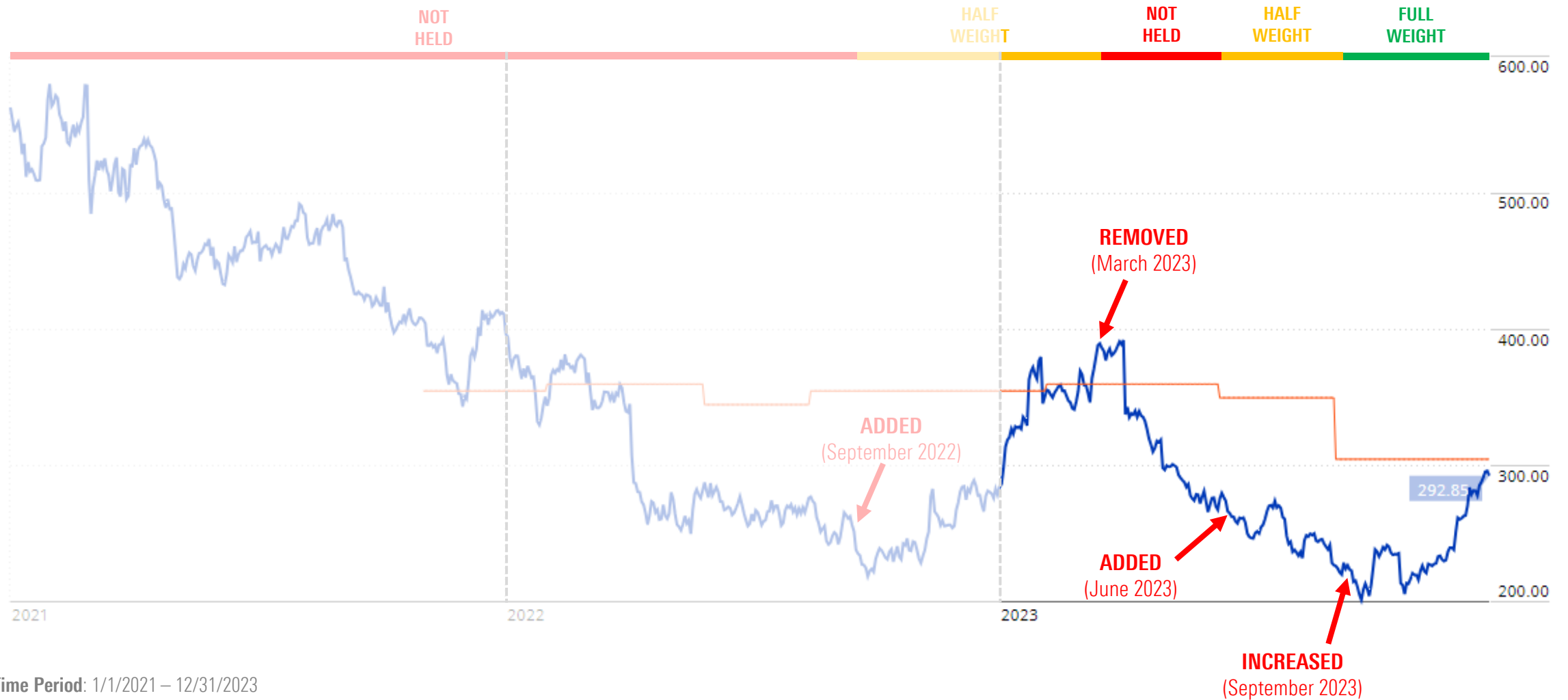


Time Period: 1/1/2021 – 12/31/2023

Source: Morningstar Direct

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Top Active Return Contributors: MarketAxess Holdings (MKTX)

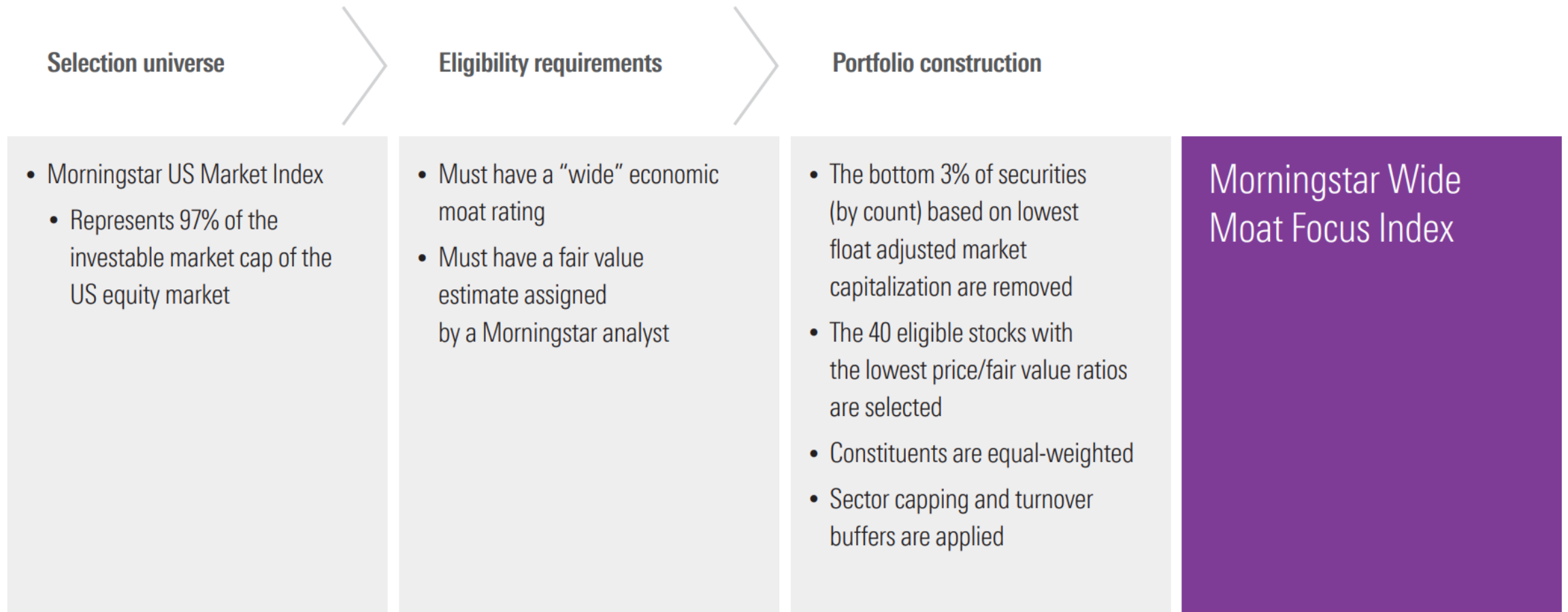


Time Period: 1/1/2021 – 12/31/2023

Source: Morningstar Direct

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Index Construction Methodology



Source: Morningstar

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