METHODOLOGY

Star Ratings are calculated by building up a score. The score is made up of three parts, and each part is calculated by reference to a benchmark for the investment. The calculations only have meaning if that benchmark provides a good basis for understanding the performance of that investment.

The process starts with finding a benchmark

The rating uses approximately 300 well-known benchmarks, including sector averages and indices, to find a 'best-fit' for each investment. Where sectors are homogenous and not too diverse, we have retained use of the sector average as a benchmark for all investments. However for more diverse sectors a best-fit, appropriate benchmark is assigned. This best fit is compared to the best-fit two years ago, to assess the persistency of the fit, and rules are applied to resolve any lack of consistency.

No investment can be expected to have a 100% correlation to its benchmark. We use the r squared coefficient to determine how much of an investment's performance is explained by the benchmark. We use this value to weight our Alpha component, the remainder is calculated using the Sortino ratio which has no requirement for a benchmark. For an investment with a perfect correlation to its benchmark the result is the Alpha value, and for an investment with a zero correlation the result is the Sortino ratio. Results in-between are done on a sliding scale based on their r squared correlation. The appropriateness of an investment's benchmark will be reviewed every two years. If it then seems that a change is appropriate, the persistency rules will still apply, to minimise changes arising from small shifts in different benchmarks' r-squared.

Next, three tests are applied – analysing alpha, volatility and consistency

Once the benchmark has been assigned, three tests are applied to the total return history of the investment. Note that three years of history is required to carry out these scores, so any investment with less history than this will not qualify for a rating.

- The alpha test

We calculate the alpha generated over the last three years, and then adjust this for the volatility of the investment. We thus make the alpha of investments more comparable, notwithstanding volatility differences, which can inflate alpha. A score is assigned on this basis.

As perfect correlation to a benchmark is not possible in most cases we use the Sortino ratio to calculate the remaining uncorrelated performance. Although similar to Sharpe ratio, Sortino measures the return to "bad" volatility without need of a benchmark, this allows a measurement of the risk adjusted returns to be made.

- The volatility test

We compare the volatility of the investment over the last three years with that of the chosen benchmark and assign a score.

- The consistency test

We look at the extent to which an investment consistently manages to outperform its benchmark over successive quarterly periods over the last three years. This is also scored, giving us three numbers to work with.

Calculating the score

Investments are grouped into eleven sub-asset classes, and for each of the tests, the raw scores are spread out in an array from zero (worst) to 100 (best).

The rescaled scores are set in proportion to the position of a investment's raw score in relation to the highest and lowest raw scores.

So there tends to be a clustering in the middle with distinctive under- and over-performers.

For each investment the rescaled results for each test are then added together.

Note that for extremely low volatility investments where minuscule volatility can seem proportionately large – Money Market, Gilts, and Index Linked Gilts – the volatility component is ignored.

Assigning an Interactive Investor Star Rating

Within each grouping, investments are given a rating based on their total scores, according to the following distribution:

- the top 10% of scores in each grouping - five stars

- the next 15% - four stars

- the next 25% - three stars

- the next 25% - two stars

- the bottom 25% - one stars

Exclusions

Investments which fit the below criteria are excluded for technical reasons:

- Investments with short history (<three years)