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## S&P Index Committee News: S&P U.S. Indices Will Move to Free Float



S&P announced on March 1st that the S&P 500, S&P MidCap 400, S&P SmallCap 600 and its other U.S. indices will adopt float-adjusted market capitalization weights. Under the plan, each company in the indices

will be weighted according to how much of its stock is available to be sold to the public.

According to David Blitzer, chairman of the S&P Index Committee, increased interest in investing outside the U.S. has raised the awareness of float issues in foreign markets where cross holdings and strategic holdings by governments or founding families are more common than the U.S. Today, most index providers have adopted free float in some form and all of S&P's non-U.S. indices are free float adjusted.

"What we've heard from many index users is that float adjustment reduces the costs of running index funds and ETFs because stocks with less float -- and therefore less liquidity -- have lower weights in the index. Index users also feel that basing the index on available shares instead of total shares means the index is a better reflection of the market and, through the market, of the economy," said Blitzer. "Our own research suggests that float adjustment would not affect the structure of S&P's U.S. indices, nor would it amend their risk profiles or sector compositions because of the liquidity in the U.S. market. In addition, the Committee has always

considered liquidity and investability in qualifying stocks for the indices."

The transition will be implemented over a fairly lengthy time period to enable the market to make changes and adjustments as easily as possible. In September 2004, the S&P Index Committee will publish procedures and float adjustment factors, and will begin calculation of provisional float-adjusted indices.

While the final implementation won't be completed until September 2005, in March 2005, the official index series for the U.S. indices will shift to partial float adjustment, using float adjustment factors that represent half of the total adjustment. Further details will be published in September 2004 on [www.indexcommitteepolicy.standardandpoors.com](http://www.indexcommitteepolicy.standardandpoors.com).

## S&P Launches Custom Index Unit

The S&P Global Custom Index Solutions group has been formed to expand S&P's custom index capabilities. This new unit, leveraging the addition of the broad S&P/Citigroup Global Equity Indices, will draw from a database that now includes more than 10,000 stocks across 75 countries. This global data set one of the broadest and deepest in the industry with free float history back to 1989.

(...continued on page 2)

## S&P Indexed Assets Survey - Trillion Dollar Tally

The results are in for the 2003 U.S. Indexed Assets Survey for S&P's indices, including the S&P 500, S&P MidCap 400, S&P SmallCap 600 and its new benchmark series, the S&P/Citigroup Global Equity Indices. Assets tied to the S&P 500 have once again exceeded the \$1 trillion mark after falling below that threshold in 2002 due to market conditions.

The survey shows a total annual growth in assets of 36%, representing \$1.2 trillion, directly indexed to S&P indices. This asset growth comes from products such as ETFs and mutual funds that directly replicate S&P indices, as well as those managed in-house by large institutional investors.

"As the market rebounded in 2003, confidence in the S&P 500 improved, while growth in indexed mid-cap and small-cap assets held steady," said Melinda Chu, director of market development, Index Services.

2003 also marked a 37% increase in assets tied to the S&P Composite 1500, the investable broad market benchmark for the U.S. equities market as it continued to gain acceptance as the index of choice among plan sponsors. -

Year End Total Indexed Assets (\$ million)  
Based on Standard & Poor's Estimates

	2003	2002	% Change
S&P 500	1,139,469	840,934	36%
S&P MidCap 400	59,432	46,105	29%
S&P SmallCap 600	22,283	18,784	19%
S&P 100	679	-	-
S&P Equal Weight	2,344	-	-
S&P ADR	449	321	40%
S&P/Citigroup Indices	12,063	-	-
<b>TOTAL</b>	<b>1,236,719</b>	<b>906,145</b>	<b>36%</b>

Full results of the survey are available in the Highlights section of [www.indices.standardandpoors.com](http://www.indices.standardandpoors.com).

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Custom indices are used by both active and index investors. Active managers, for example, might require a tailored index from which to build a specific universe of stocks for managing portfolios and measuring returns. Index managers frequently request custom solutions such as an S&P 500 that excludes certain industries or specific stocks, for example.

The S&P Custom Index Solutions group is already delivering cost-effective, independent outsourcing solutions to the market that meet investors' specific needs and mandates.

Other common examples of custom indices include geographic indices, currency-hedged indices, alternative weight indices, and net return indices, as well as fully customized indices comprising a specific set of stocks. -

## S&P/CITIC Indices for China

Standard & Poor's and CITIC Securities, one of China's leading financial and investment services companies, have successfully launched indices tracking China's A-share markets in Shanghai and Shenzhen. A-shares are shares of Chinese companies listed on those two exchanges that are open for investment by Chinese domestic investors and firms that fall under the Qualified Foreign Institutional Investors (QFII) scheme.

The S&P/CITIC 50 is designed to form the basis for index products, while the broad-market S&P/CITIC 300 index aims to provide a gauge of China's 1,200 strong A-share universe.

Two clients have been licensed to create funds based on the S&P/CITIC Indices, Harvest Fund Asset Management and Great Wall Asset Management. Great Wall Asset Management launched their fund on April 18<sup>th</sup>, while Harvest Asset Management is expected to launch later this summer.

Robert Shakotko, managing director for S&P Index Services, said S&P and CITIC would continue to develop products based on the indices. "This will not only create more choices for retail investors, but will also enhance the overall market liquidity, accelerating the growth of the Chinese equity market." -

## S&P Index Product News

- State Street Corporation is offering the **streetTRACKS S&P/ASX 200 Fund** (streetTRACKS 200) exchange-traded fund (ETF) in Japan. The streetTRACKS 200 ETF holds all of the component stocks in the S&P/ASX 200 index, which tracks the broad, investable portion of the Australian equity market.
- **Futures on the S&P/MIB Index**, began trading in March 2004. September 2004 will mark the end of MIB 30 futures and all trading and open interest will shift to the S&P/MIB.
- REFCO Securities has received SEC approval for the sale and distribution for a fund based on the **S&P Managed Futures Index Fund**. REFCO's fund is the first publicly distributed investment fund linked to an index of man-aged futures.
- The International Securities Exchange (ISE) listed **options on the S&P MidCap 400 Index** on May 25, 2004.

## O-Strip!

With the launch of the S&P 500 O-Strip Index, a new index comprised of those constituents of the S&P 500 that are primarily traded in the dealer (OTC) market, investors now have a performance measure for this subset of the S&P 500. Currently made up of 74 constituents that trade on Nasdaq, the S&P 500 O-Strip is maintained in accordance with the same index methodology as the S&P 500 and represents 15% of its market cap.

S&P is working with State Street Global Advisors on a license to create an ETF that will trade on the Amex along with options on the ETF. Futures and options on the index will also soon be available.

With this new index, investors will be able to efficiently capture the S&P 500 with fewer trades by buying the S&P 500 stocks listed on the New York Stock Exchange in a basket, and picking up the dealer (OTC) market-traded constituents through index-linked product based on the S&P 500 O-Strip.

The O-Strip can also be used by investors to isolate the dealer market securities within the S&P 500 for underweighting or over-weighting, which is a common enhanced indexing strategy.

Lastly, because the index also offers broader sector distribution than the Nasdaq 100, which excludes Financials, the O-Strip offers an alternative way to gain representative sector exposure to the dealer market, by including both financial and non-financial companies. This could appeal to investors currently using the Nasdaq 100.

Both the S&P 500 and the S&P 500 O-Strip Index are cap-weighted indices. Dividends, constituent changes and share count adjustments are treated in the same manner and implemented at the same time in the S&P 500 and the S&P 500 O-Strip Index. More information including index constituents, history and pricing can be found on [www.indices.standardandpoors.com](http://www.indices.standardandpoors.com). The ticker symbol for the index is SPOS. -

## S&P Hedge Fund Index Update: New Equity Long/Short Index

In its latest step towards increasing transparency in the hedge fund investing universe, S&P has introduced the S&P Equity Long/Short Index (SPELSI), the newest addition to the S&P Hedge Fund Index family. Building on the five Equity Long/Short funds represented in the flagship S&P Hedge Fund Index, SPELSI includes an additional 19 funds, offering a broader index of hedge funds employing this strategy.

The S&P Equity Long/Short Index includes 24 funds screened for asset size, tenure, and strategy purity. The index includes two regional sub-indices: one with a U.S. focus and one with a Global-Ex-U.S. focus, each comprising 12 funds.

Like the other hedge fund indices designed and maintained by Standard & Poor's, the S&P Equity Long/Short Index is investable through the PlusFunds separate account platform, which is designed to mirror the S&P indices. Index values, constituents and methodology are available on [www.sp-hedgefundindex.com](http://www.sp-hedgefundindex.com) and its ticker symbol is SPHGELS. -

Feature	Description
<b>Representative</b>	SPELSI is representative of the investment opportunities in Equity Long/Short strategies across regional, beta level, and beta variability spectrums, without being optimized or biased to particular criteria. Rigorous quantitative and qualitative methods are used to construct a representative index as well as select constituents.
<b>Investable</b>	The constituents of the index are required to grant capacity for new investment at the time of their inclusion in the index. The capacity of the hedge funds within the index is assessed frequently.
<b>Independent Verification</b>	Independent verification of positions is performed by a fund administrator on a daily basis.
<b>Accurate and Timely Reporting</b>	Daily publication enables timely, detailed information for analysis of volatility and correlations with other asset classes. Index values are based on the administrator's independently verified information from managed accounts. In addition, the administrator's valuations are reconciled every month with the hedge funds' valuations.
<b>Defined Due Diligence and Monitoring Process</b>	Consistent quantitative and qualitative screenings and due diligence are performed before inclusion and an ongoing monitoring process is in place to minimize single manager risk.
<b>Transparent Index Maintenance</b>	Rules governing construction and maintenance of the index, e.g., weightings, rebalancing frequency and changes to index constituents, are clear and publicly announced.

# New Index of Europe-Registered Mutual Funds: S&P ERFI

The S&P Europe-Registered Funds Indices (S&P ERFI) is a new series of three indices designed to represent actively managed mutual funds available to investors in France, Germany, Italy, and Spain. Embodying the hallmarks of S&P's index philosophy, namely the balance between representation and investability, S&P ERFI covers the European Equity, U.S. Equity, and Global Fixed Income investment markets.

"While mutual funds are a key part of the investment landscape used by a growing number of European investors, the only performance measures are broad based averages, not investable indices," said David Blitzer, managing director and chairman of the Index Committees, Standard & Poor's.

S&P ERFI provides just such an investable benchmark. The S&P ERFI series currently includes 12 funds each from European Equity, U.S. Equity, and Global Fixed Income. European Equity includes funds with investment mandates across continental Europe and the United Kingdom; U.S. Equity includes funds focused across the mid- to large capitalization markets in the U.S.; Global Fixed Income includes fixed income funds with investment mandates across major world markets. Markets under considera-

tion for subsequent index coverage include Japanese/Asian Pacific Equities and Emerging Markets.

Under the oversight of an S&P Index Committee, S&P ERFI constituents are selected from a broad universe of funds in the proprietary Standard & Poor's Funds database. The funds are screened to identify those that have a high correlation to their peers, thereby improving representativeness and have a minimum three-year track record.

In addition, to facilitate investability, all index candidates must be UCITS-compliant and registered for sale in France, Germany, Italy, and Spain. The candidates then undergo a qualitative review that includes examination of manager/team tenure and experience, organizational depth, fund philosophy and process, style consistency, tracking results to benchmarks and other factors as appropriate.

The S&P ERFI series daily index values with a one-day lag are available on our website, as well as via Bloomberg tickers SPERFIEE, SPERFIUS, and SPERFIFI. More information about the construction methodology, index history, and constituents is available on [www.indices.standardandpoors.com](http://www.indices.standardandpoors.com). -

## SPIVA Japan

Building on the successful index versus active funds scorecard produced quarterly in the U.S. (see [www.spiva.standardandpoors.com](http://www.spiva.standardandpoors.com)), S&P is now publishing SPIVA (Standard & Poor's Index Versus Active Funds Scorecard) Japan. Like its U.S. counterpart, the scorecard represents semi-annual performance data for Japanese domestic equity mutual funds benchmarked against the components of the S&P Japan 500 index series.

"SPIVA Japan provides a new dimension on the Japanese mutual fund industry and because of the compatibility of the methodology for S&P's global indices, investors can now compare the Japanese fund industry's performance with that of the U.S. in a new and meaningful way," said Seiichiro Uchi, Senior Director, Standard & Poor's (Japan).

Overall, results for the semi-annual period from June 2003 to January 2004 showed that active funds have difficulty outperforming the market in Japan over the long term. In the three and five year categories, actively managed funds fared much worse than their index counterparts, outperforming indices just 32.5% and 29.61% of the time, respectively.

Over shorter time horizons however, results varied. In the large-cap category, active funds and indices were almost at a dead tie with 50.7% of active funds outperformed by the S&P/TOPIX 150 index.

In the small-cap arena, performance varied greatly depending on the timeframe examined. For example, while over the most recent two-quarter period, active funds beat the S&P Japan SmallCap 250 index almost 91% of the time, over longer time horizons, such as the 3-year and 5-year periods, this dropped to 28% and 51%, respectively.

When comparing SPIVA Japan results against those in the SPIVA U.S., the percentage of active funds that beat the index benchmark in the U.S. is higher than in Japan. For example, during the past five years, while approximately 50% of U.S. actively managed equity funds outperformed the S&P Composite 1500, only 38% of Japanese active funds beat the S&P Japan 500.

"This kind of cross-market comparison offers new insight into international investing and we intend to further analyze the mutual fund industry in both markets," said Uchi. -

## Meet Steve Rive

Stephen Rive has recently joined Standard & Poor's as vice president, Standard & Poor's Index Services (Canada) and global head of exchange-listed products. Based in Toronto, Steve has global responsibility for overseeing and expanding development of exchange-listed products based on S&P indices, and heads the index business in Canada.

Steve joins S&P from Barclays Global Investors in Canada where he oversaw the firm's public funds business, including the creation of the iUnits family of exchange-traded funds (ETFs) and the Barclays Funds line of closed-end, exchange-traded, structured products. Among his other product innovations in this role were the world's first fixed income ETFs and the first synthetic ETFs. Prior to that Steve spent more than 10 years working at stock exchanges in Canada and the Far East. -

