

# INDEX BULLETIN

## S&P Free Float Transition

On March 1, 2004 Standard & Poor’s announced that its US index series would be shifting to a free float adjusted capitalization methodology. Due to the magnitude of the trading activity necessitated by the methodology revision, S&P used a two phase implementation process. These changes impacted the S&P 500, S&P MidCap 400, S&P Small Cap 600 and their respective style indices. Below is the time line indicating the modification schedule for the indices.

- October 15, 2004 Published provisional half-float and full-float indices
- March 18, 2004 (Phase I) Indexes shifted to half-float indexes
- September 16, 2005 (Phase II) Completion of shift to full-float methodology

On the close of September 16, 2005, the combined quarterly share change, annual float change and phase II of the S&P trade occurred. The following is an overview our implementation and analysis.

### Implementation & Analysis

The second phase of the S&P free float transition behaved as expected. The portfolio of stocks that needed to be purchased increased during the day while the portfolio of stocks to be sold decreased. Critical analysis of the spread of the two portfolios is essential as it greatly affects the transition cost the fund absorbs as a result of an index change. The pattern persisted in the S&P 500 (Figure 1) as the spread between the buys and sells steadily increased during the day. The S&P 400 (Figure 2) began on a similar path, however, the index experienced a mid-day dip, as the portfolio of buy stocks dropped and the sell stocks climbed. This trend did reverse within the last 30 minutes of the trading day. Careful analysis of the movement of the various portfolios and a trading strategy that shifted the risk to our brokers while retaining upside participation allowed us to minimize the wealth effect of this event thus maximizing returns relative to the benchmark.

Figure 1: S&P 500 Buy/Sell Spread during Phase I and Phase II trade day

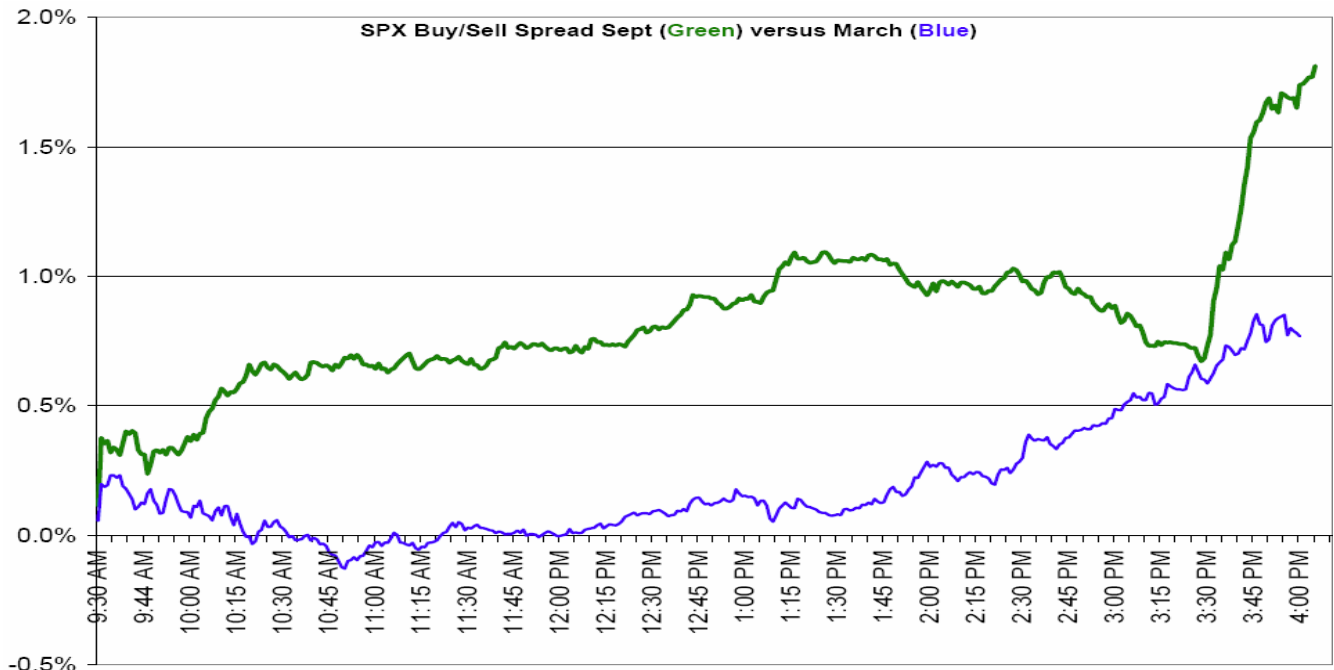
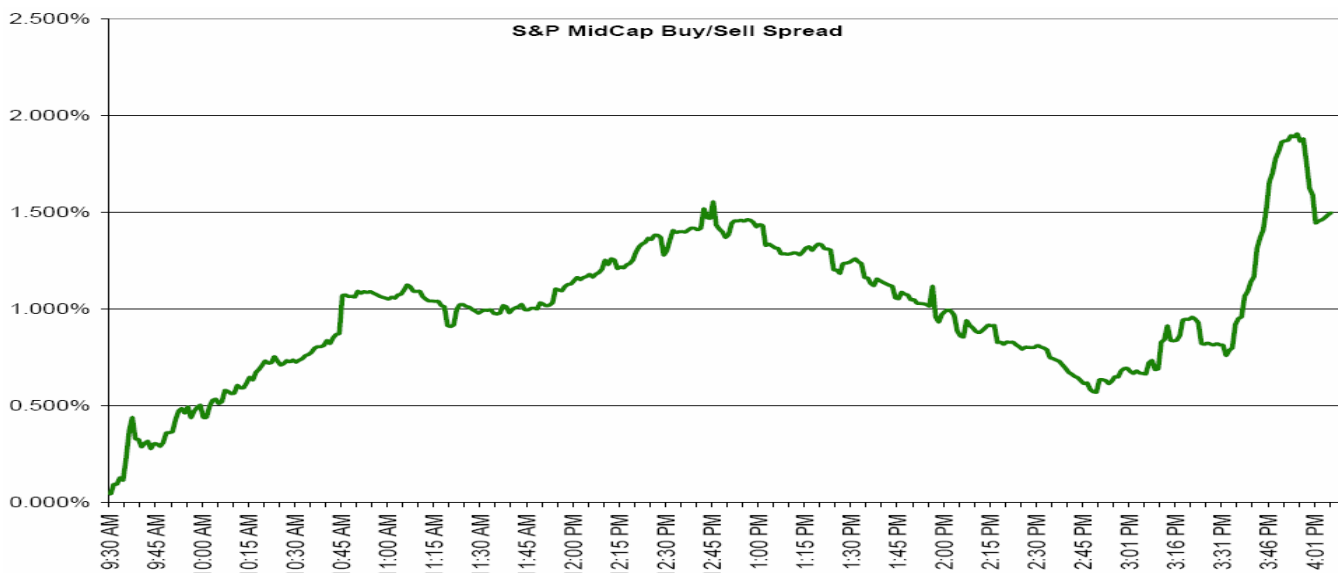


Figure 2: S&P MidCap 400 Buy/Sell spread on September, 16 2005



**Turnover Analysis**

As indicated above, the transition to the full float methodology was spread out in two phases, March and September 2005. Standard & Poor’s began publishing provisional half float and free float performance numbers in October 2004, giving investors the option to transition early. As a result of the two phase transition, the two-way turnover for September in the S&P 500, S&P 400 and S&P 600 were 3.18%, 4.38% and 4.4% respectively. The chart below includes the names of the largest buys and sells within the S&P 500, S&P MidCap 400 and S&P SmallCap 600.

Figure 3: Largest Buys and Sells - Phase II trade day

S&P 500		S&P MidCap 400		S&P SmallCap 600	
Top 5 Buys	Top 5 Sells	Top 5 Buys	Top 5 Sells	Top 5 Buys	Top 5 Sells
General Electric	Wal-Mart Stores	Peabody Energy	Boyd Gaming Corp.	Moog Inc. Cl. 'A'	MGI PHARMA, Inc.
American Express	Microsoft Corp.	Sierra Pacific (New)	Hormel Foods Corp.	NETGEAR Inc.	Burlington Coat Factory
Goldman Sachs Group	Oracle Corp.	Community Health Systems	PepsiAmericas, Inc.	Unit Corp.	Florida Rock Industries
Johnson & Johnson	Coca Cola Co.	Barr Pharmaceuticals, Inc.	Washington Post	New Century Financial Corp.	Electronics Boutique Hldgs Corp.
Exxon Mobil Corp.	News Corporation	MEMC Electronic Materials	Hovnanian Enterprises Inc.	NVR, Inc.	M.D.C. Hldgs

If you have any questions about this index event or an interest in discussing the S&P free float adjustment further, please contact the Global Quantitative Strategy Group or your Investment Relationship Manager.

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