



# ETF Investing

## NYSE EXCHANGE-TRADED FUNDS EXPAND OPPORTUNITIES FOR INVESTORS

A diversified, low-cost and tax-efficient basket of securities all in a single trade — that’s the benefit exchange-traded funds (ETFs) deliver to investors, explains Lee Kranefuss, CEO of the Intermediary & Exchange Traded Funds business at Barclays Global Investors, known as BGI, a division of **Barclays plc** (BCS).

Kranefuss was at the NYSE this spring to celebrate the listings of two new ETFs: **iShares® NYSE Composite Index Fund** (NYC) and the **iShares NYSE 100 Index Fund** (NY), the first to be based on the NYSE’s own indexes. Both, says NYSE President Catherine Kinney, provide access to the quality and diversity of NYSE issuers in a single security “for efficient and immediate diversification.”

The NYSE Composite Index® measures the performance of all listed common stocks, ADRs, REITs and tracking stocks. With a market cap of \$15 trillion, the NYSE Composite companies represent 78 percent of the U.S.’s total market cap and 66 percent of the world’s. “That’s really broad exposure,” says Kranefuss.

A subset of the NYSE Composite, the NYSE U.S. 100 Index™ is a performance measure of the Exchange’s 100 largest U.S. stocks by market cap. Both offer much larger market caps and lower volatility than peer indices (see chart, next page). “Both funds represent established, stable companies,” Kranefuss says. “The NYSE stands for high-quality listings — companies you know you can trust.” Kranefuss also was on hand this summer for the listings of nine new iShares Morningstar Index ETFs:

- **iShares Morningstar Large Core Index Fund** (JKD),
- **iShares Morningstar Large Growth Index Fund** (JKE),
- **iShares Morningstar Large Value Index Fund** (JKF),
- **iShares Morningstar Mid Core Index Fund** (JKG),
- **iShares Morningstar Mid Growth Index Fund** (JKH),
- **iShares Morningstar Mid Value Index Fund** (JKI),
- **iShares Morningstar Small Core Index Fund** (JKJ),
- **iShares Morningstar Small Growth Index Fund** (JKK), and
- **iShares Morningstar Small Value Index Fund** (JKL).

The Exchange now lists 16 ETFs, including:

- **iShares S&P Global 100 Index Fund** (IOO), which tracks the performance of the S&P Global 100 Index;
- **streetTRACKS™ Dow Jones Euro STOXX 50 Fund** (FEZ) and the **streetTRACKS Dow Jones STOXX 50 Fund** (FEU), which are based on the most widely used European market indexes;
- **iShares Dow Jones Select Dividend Index Fund** (DVY), which is based on dividend-yielding investments only; and
- **iShares Lehman TIPS Bond Fund** (TIP), which tracks the performance of the U.S. Treasury Inflation Notes Index.

The NYSE also trades 36 ETFs on an unlisted trading privileges (UTP) basis, including the Nasdaq-100 Index Tracking Stock® (QQQ), Standard & Poor’s Depository Receipts® (SPY) and The Dow Industrials DIAMONDS® (DIA). The Securities Exchange Act of 1934 permits securities listed on any national securities exchange to be traded on a UTP basis by other such exchanges.

**INVESTORS  
AND INTERMEDIARIES  
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### BENEFITS FOR INVESTORS

ETFs represent a diversified basket of stocks reflecting the performance of a market

index, industry, sector, style or region. ETFs can track stock indexes, bond indexes and other market measures.

Individuals, institutions and intermediaries, say they find ETFs attractive because of their trading flexibility and continuous pricing. ETFs trade intraday on stock exchanges at market-determined prices and are bought and sold like common stocks. (In contrast, mutual funds are bought and sold at the end of the trading day at their end-of-day net asset value.) Investors can buy, sell and hold ETF shares through a brokerage account.

“Because we believe in efficient markets and a passive strategy, ETFs immediately garnered our interest,” says Dennis Covington, vice president of Capital Directions in Atlanta, which manages \$275 million in assets, of which about \$36 million is invested in ETFs, he says. The “clearest benefit,” he adds, “is tax efficiency.” Covington says his firm uses ETFs in taxable and tax-deferred accounts. “We bought ETFs in

1999-2000 and have held them since with no capital gains distributions.”

Additional product features are no investment minimums and relatively low expense ratios. The management fees for the iShares NYSE Composite Index Fund and the iShares NYSE 100 Index Fund are 25 and 20 basis points, respectively.

### BENEFITS FOR UNDERLYING ISSUERS

For issuers, inclusion in an index on which an ETF is based can lead to whole new sets of investors. “The ETF is often the means to attracting new demand for the securities in that fund,” Kranefuss explains. “Occasionally,” he adds, “CEOs of the underlying companies will come up to me and say, ‘Thanks for including us. We’re seeing more demand for our stock that otherwise would be hard for us to reach.’”

According to William Margaritis, **FedEx Corp.**’s (FDX) senior vice president of Worldwide Communications and Investor Relations, being added to the NYSE U.S. 100 index in December 2003 means “more investors will pay attention to FedEx, and the visibility will stimulate demand for our stock.”

But the visibility, he says, is only part of the benefit: “We’re proud to be joining a stellar group of companies that have consistently delivered superior shareholder value. Communicating this inside our organization helps build morale among our 245,000 employees worldwide.”

The new NYSE funds also evidence ETFs’ growing popularity. According to **Morgan Stanley** (MWD), the 132 ETFs in the U.S. had \$161.3 billion in assets as of March 31, up from 117 ETFs with \$150.7 billion in assets at year-end 2003. During the first-quarter 2004, average daily trading volume in ETFs globally was also up, by 64 percent

in dollar terms and 50 percent in number of shares, Morgan Stanley reports. BGI, the largest ETF manager globally, said that in 2003 it witnessed almost 50 percent asset growth in the overall ETF industry and 71 percent growth in its own iShares fund family.

Still, says Kranefuss, ETF assets account for only 2 percent of all mutual fund assets, so “our big challenge is education — getting investors to understand the ETF benefits. The NYSE can help us do that given its cachet with influencers.”

Michael Latham, COO of BGI’s Intermediary & Exchange Traded Funds business, adds that the strength of the NYSE brand should contribute to ETFs’ appeal: “The NYSE is a premier brand. Putting its name behind these products is an indication that the world’s largest exchange believes in ETFs and will continue growing its presence in this industry.”

To help investors understand and track broad markets, the Exchange has created several other indexes, though none are yet the basis for ETFs:

- The NYSE International 100 Index,<sup>SM</sup> which measures the performance of the NYSE’s 100 largest non-U.S. stocks by market cap,
- The NYSE World Leaders Index,<sup>SM</sup> which includes all the components of the NYSE U.S. 100 and International 100 Indexes, and
- The NYSE TMT Index,<sup>SM</sup> which tracks the performance of the NYSE’s 100 largest technology, media and telecom companies.

Recently, the Exchange introduced three sector indexes — the NYSE Energy Index,<sup>SM</sup> the NYSE Financial Index<sup>SM</sup> and the NYSE Healthcare Index. All are capitalization-weighted, adjusted for free-float shares, and calculated and maintained by Dow Jones Indexes, a unit of **Dow Jones & Co. Inc.** (DJ). Values are published every business day. (For more information, visit [www.nyseindexes.com](http://www.nyseindexes.com) and [www.nyse.com/etf](http://www.nyse.com/etf).) □

### COMPARISON OF INDEX PRODUCTS BY MARKET CAP AND VOLATILITY

| MARKET INDEX                | MARKET CAP      | % OF TOTAL MARKET CAP |       | MARKET INDEX                           | VOLATILITY |
|-----------------------------|-----------------|-----------------------|-------|----------------------------------------|------------|
|                             |                 | U.S.                  | WORLD |                                        |            |
| NYSE Composite              | \$14.2 trillion | 78%                   | 66%   | NYSE Composite*                        | 14.2%      |
| Nasdaq Composite            | \$3.2 trillion  | 22%                   | 15%   | Nasdaq Composite*                      | 28.7%      |
| Dow Jones U.S. Total Market | \$11.6 trillion | 94%                   | 53%   | Dow Jones U.S. Total Market*           | 16.0%      |
| S&P 500                     | \$9.7 trillion  | 78%                   | 44%   | S&P 500*                               | 15.7%      |
| NYSE 100                    | \$5.8 trillion  | 46%                   |       | NYSE 100 <sup>§</sup>                  | 15.4%      |
| Nasdaq 100                  | \$1.7 trillion  | 14%                   |       | Nasdaq 100 <sup>§</sup>                | 40.2%      |
| Dow Jones Industrial Avg.   | \$3.0 trillion  | 24%                   |       | Dow Jones Industrial Avg. <sup>§</sup> | 17.3%      |
| S&P 100                     | \$5.5 trillion  | 44%                   |       | S&P 100 <sup>§</sup>                   | 18.6%      |

\*ANNUALIZED FIGURES BASED ON MONTHLY RETURNS OVER THE PAST 10 YEARS. §ANNUALIZED FIGURES BASED ON MONTHLY RETURNS OVER THE PAST FIVE YEARS. SOURCE: FACTSET. DATA AS OF 12/31/03.