

Trustworthy News

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“Growing and Preserving Your Wealth...”



All About Indices

No doubt you've seen headlines reporting that a particular index is up or down. But do you know how an index works, and why understanding the nuts and bolts of a specific index can make a difference to your portfolio?



An index is simply a way to measure and report the fluctuations of a securities market or a particular segment of a market. An index is developed by a company that sets specific criteria to determine which securities are included in the index—factors such as a company's size or location, or the liquidity of its stock. For example, the S&P 500 is a collection of large-cap U.S.-based companies that Standard and Poor's considers to be leading representatives of a cross section of industries.

The company that develops the index tracks the performance of its components and aggregates the data to produce a single figure that represents the index as a whole. Virtually every asset class has at least one index that tracks it, but because of the size and variety of the stock mar-

ket, there are more stock indexes than any other type.

How indices are used

In addition to providing valuable information needed to monitor how a particular market is faring, an index can serve as the basis for mutual funds or exchange-traded funds that attempt to replicate its performance; that process is known as indexing. An index also can be used as a benchmark for funds that invest in the same asset class, regardless of whether a fund includes the same specific securities. Finally, some investment products do not attempt to replicate an index's performance but represent a bet on the index's general movements, though such investments can be challenging and are not appropriate for every investor.

You can't invest in an index

You cannot invest directly in an index. You could always purchase each and every security in the index and do the necessary trading to ensure that the portfolio continues to mirror the index, but the financial services industry has saved you the trouble. As noted above, investment products such as index mutual funds and exchange-traded funds are used by investors to try to capture a particular market's performance.

However, an index-based investment may not match the return of an index exactly. One reason is what's known as "tracking error." Costs such as taxes, operating expenses (even minimal ones), and transaction costs

can differ among mutual funds. As a result, your return may be slightly different from that of the index or even other funds based on the same index, even though most index funds try to keep tracking error to a minimum.

Indices don't stay static

Though an index adheres to a set of guidelines for selection of the securities it includes, the company that oversees the index generally reviews the security selection periodically. For example, some indices are rebalanced if an individual security grows so large that it dominates the index. Others have a limit on how much of the index can be devoted to a particular sector or industry, and rebalance if the proportion gets skewed. And in some cases, an index is altered because of serious problems with one of its components (for example, Flowserve Corp. replaced Washington Mutual Inc. in the S&P 500 after WaMu was closed by the Office of Thrift Supervision in 2008).

Weight watching

Even indices that include the same securities may not operate in precisely the same way. Why? Because different indices may weight the relative importance of the same securities in different ways. The way an index is weighted determines how much of each individual security is included in it—for example, how many shares of stock. That weighting in turn can affect the overall index's performance.



Reliance Investments and Insurance

To round out Reliance's product offerings, Zeb Jackson, serves as the Investment Advisor Representative in our brokerage division. Zeb's responsibilities include assisting individuals and families in achieving their financial goals through: Investment Management, Insurance Planning, Education Planning, Financial Planning and Wealth Management.



Jackson received a Bachelor of Science degree from Bowling Green State University and currently holds securities series 6, 65, and 7 licenses in addition to Life Insurance and Annuity licenses.

Jackson states, "What we do most, is simplify financial complexities for those that don't have the time or financial expertise to do it themselves. We take a holistic approach, by gaining a greater understanding of our clients complexities. We coordinate with not only our clients, but also, their tax and legal advisors to make sure we're all on the same page and moving in the right direction. Once we have collaborated with our clients and our team of experts, we create a blueprint utilizing the right mix of products that will give our clients and their families the true greatest opportunity to realize their financial goals. Lastly, we continuously monitor and make

appropriate adjustments as our clients go through life changes."

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Please contact Zeb Jackson for more information. Zeb is available to meet with you at any State Bank branch in Northwest Ohio, your place of business, or your home. You may contact him by phone or email as listed below.

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Some indices are weighted based on market capitalization; the companies with the highest market cap (total value of stock outstanding) make up a larger share of the index than companies with a smaller market cap. As a result, those companies can have a disproportionate impact on the performance of an index weighted by market cap. For example, a 10% decline in the price of the largest company in the S&P 500 index would affect the index's overall return more dramatically than a 10% drop in the price of a much smaller company, because the S&P 500 is weighted by market cap.

Other indices are weighted by price; the most expensive stocks receive greater weight than lower-priced stocks. The Dow Jones Industrial Average, which includes 30 large, blue-chip industrial stocks and is commonly referred to as the Dow even though there are several Dow indices, is price-weighted. A relatively new approach to weighting an index is to use certain fundamental attributes, such as dividends or cash flow, as the basis for weighting the stocks that comprise the index.

To produce a figure that indicates the value of the aggregated securities, an index divisor is typically applied to produce a more manageable figure that is easier to quote than the index's actual value