

Document 1600

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When it comes to buying and selling shares , Westridge Capital Management Inc. takes a back seat to no one .

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Every dollar 's worth of stock in the Los Angeles money manager 's portfolio is traded seven or eight times a year , the firm estimates .

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That makes it the most active trader among all the nation 's investment advisers , according to Securities and Exchange Commission filings .

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But wait a second .

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Westridge Capital is an index fund - the type of stolid long-term investor whose goal is to be nothing more than average .

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Westridge Capital 's frenetic trading reflects the changes sweeping through the previously sleepy world of indexing .

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Indexing for the most part has involved simply buying and then holding stocks in the correct mix to mirror a stock market barometer , such as Standard & Poor 's 500-stock index , and match its performance .

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Institutional investors have poured \$ 210 billion into stock and bond indexing as a cheap and easy form of investment management that promises to post average market returns .

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These big investors have flocked to indexing because relatively few " active " stock pickers have been able to consistently match the returns of the S&P 500 or other bellwethers , much less beat it .

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That 's because computers do most of the work , and low trading activity keeps a lid on commission costs .

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But today , indexing is moving from a passive investment strategy to an increasingly active one .

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Because index-fund managers are no longer satisfied with merely being average , they have developed " enhanced " indexing strategies that are intended to outperform the market as much as three percentage points .

[21600014]

Indexing has been the most single successful investment concept in the last decade, but the index money has been just sort of sitting there," says Seth M. Lynn, president of Axe Core Investors Inc., an indexer based in Tarrytown, N.Y.

Among the souped-up indexing strategies: Indexed portfolios can be built around thousands of stocks, or just a few dozen, rather than being restricted to the S&P 500 companies.

They can ignore the S&P 500 stocks altogether and focus on particular types of stocks, such as smaller companies, those paying high dividends or companies in a particular industry, state or country.

With today's computer-driven program trading techniques, index funds can trade back and forth between stock-index futures and the actual stocks making up indexes such as the S&P 500.

Futures and options also make it possible to build "synthetic" index funds that do n't actually own a single share of stock, but can produce returns that match or exceed the broad stock market.

One reason for these hybrids is that indexing's rapid growth is slowing, particularly for those "plain vanilla" funds that mirror the S&P 500.

(After tripling in size in the past five years, index funds now hold about 20 % of the stock owned by pension funds.)

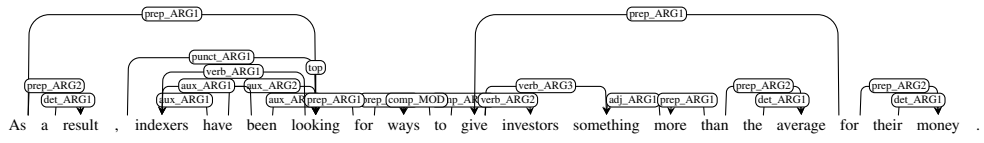
A further problem is razor-thin profits.

Plain-vanilla funds have become so commonplace that fees they can charge have plunged to almost nothing, and in some cases are just that.

To land customers for their well-paying stock custodial business, big banks sometimes will throw in basic indexing services for free.

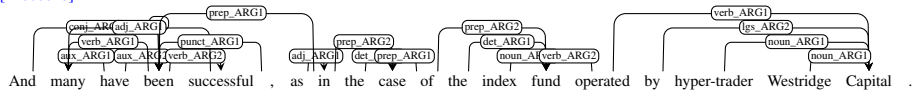
"It's like getting a free toaster when you open an account," says Axe Core's Mr. Lynn.

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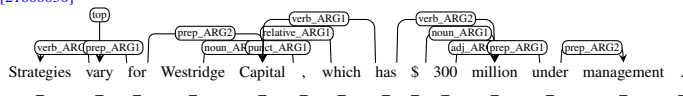
As a result , indexers have been looking for ways to give investors something more than the average for their money .

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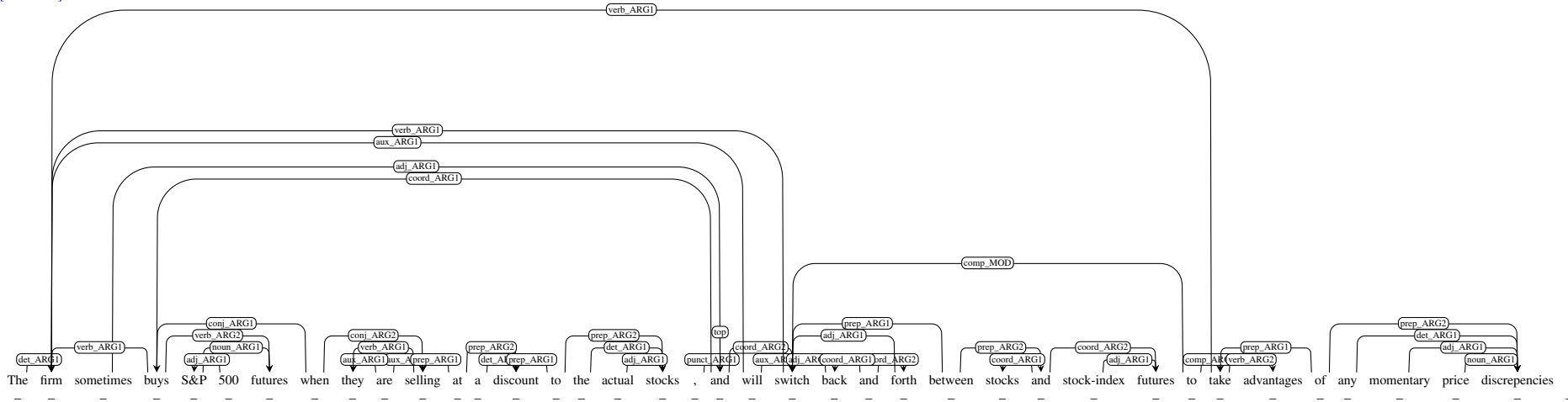
And many have been successful , as in the case of the index fund operated by hyper-trader Westridge Capital .

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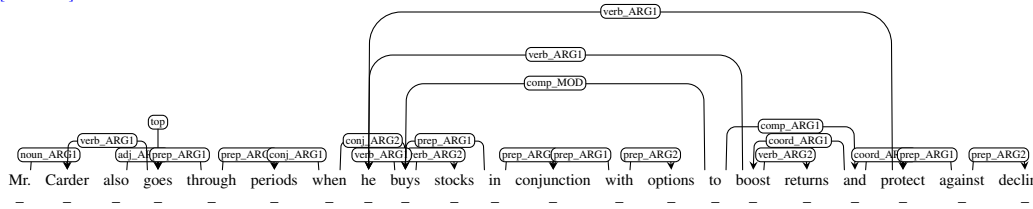
Strategies vary for Westridge Capital , which has \$ 300 million under management .

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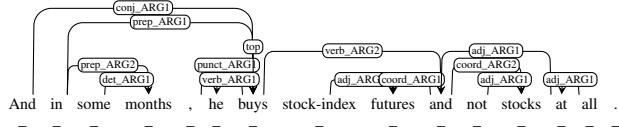
The firm sometimes buys S&P 500 futures when they are selling at a discount to the actual stocks , and will switch back and forth between stocks and stock-index futures to take advantages of any momentary price discrepancies .

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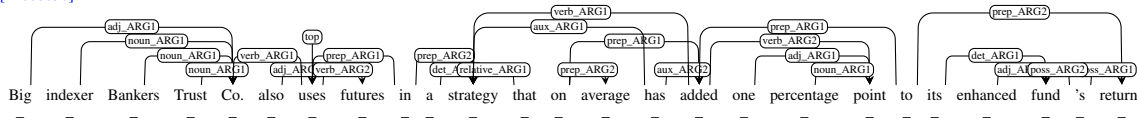
Mr. Carder also goes through periods when he buys stocks in conjunction with options to boost returns and protect against declines .

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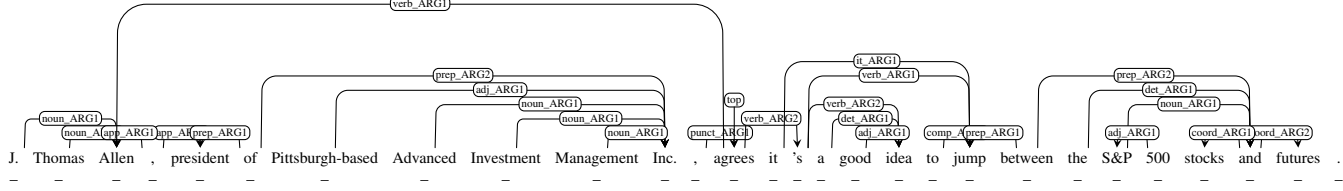
And in some months , he buys stock-index futures and not stocks at all .

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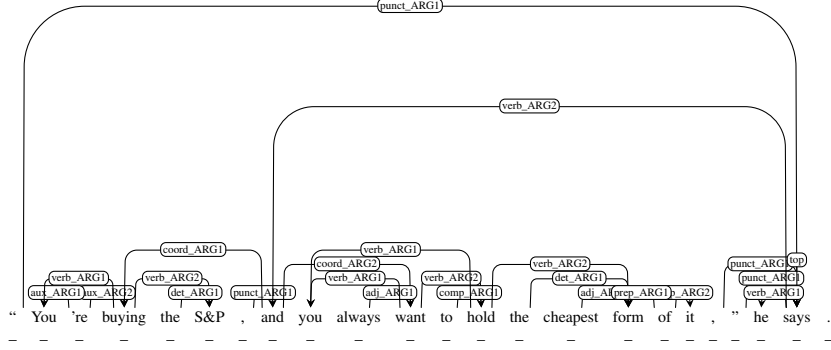
Big indexer Bankers Trust Co. also uses futures in a strategy that on average has added one percentage point to its enhanced fund 's returns .

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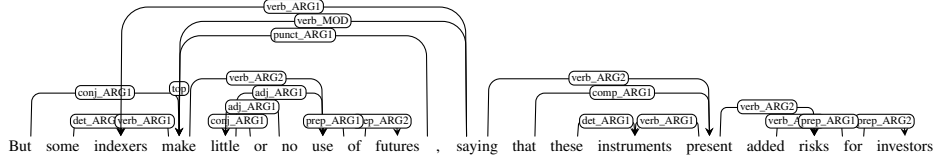
J. Thomas Allen , president of Pittsburgh-based Advanced Investment Management Inc. , agrees it 's a good idea to jump between the S&P 500 stocks and futures .

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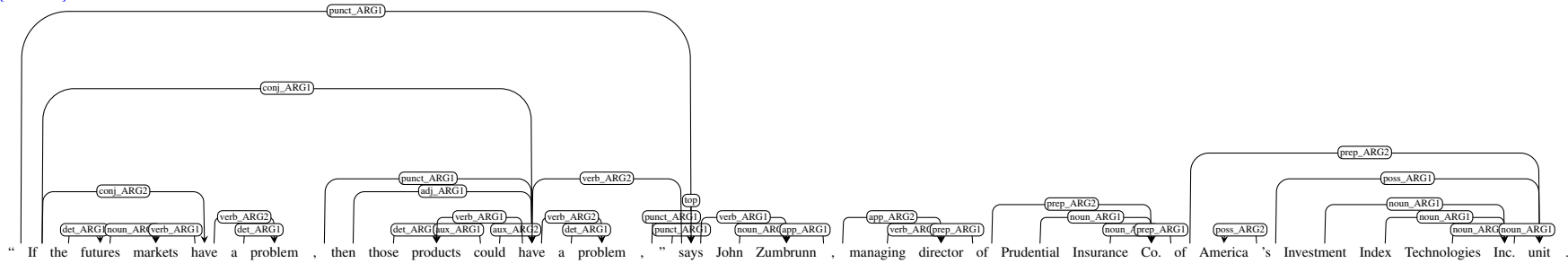
" You 're buying the S&P , and you always want to hold the cheapest form of it . " he says .

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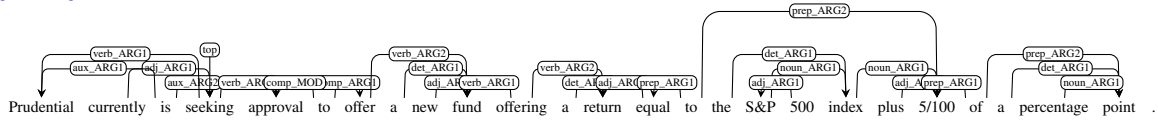
But some indexers make little or no use of futures , saying that these instruments present added risks for investors .

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" If the futures markets have a problem , then those products could have a problem . " says John Zumbunn , managing director of Prudential Insurance Co. of America 's Investment Index Technologies Inc. unit .

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Prudential currently is seeking approval to offer a new fund offering a return equal to the S&P 500 index plus 5/100 of a percentage point .

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