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# Exchange Traded Funds in India

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**ABSTRACT - ETF is the medium or instrument in the market with which small units of shares or commodities is purchased or sold. These can be based on index commodities, bonds or a basket of assets like an index fund. For example: If 1kg gold is equal to rupees 30 lakhs, then, 1 ETF, even, may be equal to 1 gm. ETF are listed on stock exchanges and traded like general stock. Retail investors can purchase these through their trading account. ETFs offer both tax efficiency as well as lower transaction and management costs.**

***Keywords: ETF, NASDAQ, NSE, Retail investors, Stock Exchange, Trading account***

## I. INTRODUCTION

ETFs made their first recognition in 1989 with Index Participation Shares, an S&P 500 proxy was traded on the American Stock Exchange and the Philadelphia Stock Exchange. The product, disappeared soon after a lawsuit by the Chicago Mercantile Exchange. A parallel product, Toronto Index Participation Shares was launched on the Toronto Stock Exchange (TSE) in 1990. The shares, which tracked the TSE 35 and later the TSE 100 indices, evidenced to be popular. The popularity of these products encouraged the American Stock Exchange to try to develop something that would satisfy SEC regulation in the United States.

Nathan Most and Steven Bloom innovated Standard & Poor's Depositary Receipts (NYSE Arca: SPY), introduced in January 1993. Popularly known as SPDRs or "Spiders", the fund became the prime ETF in the world. In May 1995 they launched the MidCap SPDRs (NYSE Arca: MDY). Barclays Global Investors which was a subsidiary of Barclays PLC, in aggregation with MSCI and as its underwriter, i.e., Funds Distributor Inc., stepped in the market in 1996 by means of World Equity Benchmark Shares (WEBS), which became quite popular as iShares, MSCI Index Fund Shares. WEBS were mainly innovative because they offered casual investors easy access to foreign markets. Unlike, SPDRs which were organized as unit investment trusts, WEBS were set up as a mutual fund, the first of their own kind.

In 1998, State Street Global Advisors introduced "Sector Spiders", that follow nine sectors of the S&P 500. Also in 1998, the "Dow Diamonds" (NYSE Arca: DIA) were announced, tracing the famous Dow Jones Industrial Average. In 1999, the influential "cubes" (NASDAQ: QQQ), were launched to make an effort to replicate the movement of the NASDAQ-100. The iShares line was introduced in early 2000. Within five years iShares had exceeded the assets of any other ETF opponent in the U.S. and Europe. Barclays Global Investors was purchased by BlackRock in 2009. The Vanguard Group stepped in the market in 2001. The first fund was Vanguard Total Stock Market ETF (NYSE Arca: VTI), which had become fairly popular, and they made the Vanguard Extended Market Index ETF (VXF). Some of Vanguard's ETFs are a share class of a prevailing mutual fund.

iShares made the foremost bond funds in July 2002, founded on US Treasury bonds and corporate bonds, like iShares iBoxx $ Invst Grade Crp Bond (LQD). They also created a TIPS fund. In 2007, they presented funds based on junk and muni bonds; about the same time SPDR and Vanguard got in gear and innovated several of their bond funds. Since then ETFs have grown, personalized to a gradually definite array of regions, sectors, commodities, bonds, futures, and other asset classes. On January 2014, there were over 1,500 ETFs dealt in the U.S., with over $1.7 trillion in assets. In December 2014, U.S. ETF assets pass on above $2 trillion. [1]

***Different types of ETFs:***

1. Index ETFs
2. Stock ETFs
3. Bond ETFs
4. Commodity ETFs
5. Currency ETFs
6. Actively managed ETFs
7. Exchange-traded grantor trusts
8. Inverse ETFs
9. Leveraged ETFs

***Objectives of study:***

- ✓ To study the importance of ETFs in Indian markets.
- ✓ To study the benefits of ETFs over other securities.
- ✓ To find out how ETFs works in market.
- ✓ To observe the performance of different ETFs.

## II. METHODOLOGY

The study is descriptive in nature and secondary sources of information like websites, browser, e-papers and books are used to draw conclusions

***ETFs in India:***

ETFs are launched in 2002 in India after it came in news on Dec 14,2001 "Investors can now buy a Nifty replica with one single decision. Nifty BeES, can be bought or

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sold like any other stock on the exchange through brokers. The Fund will be listed on the NSE on January 8" These are traded on different stock exchanges in India. Popular ETFs in India are: Equity ETFs, Commodity ETFs, Date ETFs etc.

1. Equity ETF: These are launched in 2002 in India. But after 2013, when these are linked to govt. company's index these become very popular among investors. More than 30 ETFs are listed on NSE. The investor invests in whole index without falling in the complexity of derivatives. The fund can be invested for a maximum period of three months in futures, but, in ETF investor can invest up to their will.
2. Commodity ETF: These are launched in 2007 with gold ETF in India. They become very popular in 2009, but in 2013, when gold rate decline, they become less preferred. There are number of benefits of ETF. Fear of displacement of instrument does not exist due to demat account. The price is set by London bullion market. 13 gold ETF are listed on NSE.
3. Date ETF: By investing in Date ETF the investor can invest in govt. securities and bonds in small amounts. Generally, when investor have no idea of where to invest, they select Date ETF. 2 Date ETF are listed on NSE. [2]

***ETF Creation and Redemption***

The regulation of stock of ETFs is done through a procedure of creation and redemption. The procedure of creation/redemption comprises of few large specialized stockholders, known as authorized participants (APs). APs are big financial organizations with a high degree of purchasing power, such as market makers that might be banks or investment concerns.

Only APs can create or redeem units of ETFs. While creating ETFs, an Authorised Participant assembles the portfolio of underlying assets and turns that basket over to the fund in stock exchange for afresh created ETFs and during redemptions, APs return back ETFs to the fund and collect the basket consisting of the underlying portfolio. Every day, the fund's underlying assets are unveiled to the public.

***ETFs and Traders***

ETFs and the basket of underlying assets are traded whole day and traders perform arbitrage process resulting the ETFs price to be closed at justified value. If a trader can purchase the ETF for efficiently less than the underlying securities, they will purchase the ETFs and sell the underlying portfolio, locking in the differential.

Some ETFs employ gearing, or leverage, through the practice of derivative products to create inverse or leveraged ETFs. Inverse ETFs track the reverse return of that of the underlying assets – for example, the inverse gold ETF would increase 1% for every 1% decrease in the price of the metal. Leveraged ETFs seek to gain a manifold return of that of the underlying. A 2x gold ETF would increase 2% for every 1% increase in the price of the metal. There can also be leveraged inverse ETFs such as negative 2x or 3x return portfolio. [3]

***How ETF Works***

Whenever an investor purchases an ETF, he or she is fundamentally investing in the performance of an underlying bundle of securities -- generally those representing a particular index or sector. Unit Investment Trusts (UITs) are often organized in the same style. Though, the unfamiliar legal structure of an ETF makes the product somewhat exclusive.

Exchange-traded funds don't sell shares directly to stakeholders. As an alternative, each ETF's sponsor issues large blocks (often of 50,000 shares or more) that are recognized as creation units. These units are then purchased by an "authorized participant" -- typically a market maker, specialist or institutional investor -- which acquires shares of the underlying securities and put them in a trust. The authorized participant then splits up these creation units into ETF shares -- each of which signifies a legal claim to a minute fraction of the assets in the creation unit -- and then sells them on a secondary market.

Just like closed-end funds don't always trade at a price that indeed reflects the value of the underlying assets in each share of the portfolio, it is also probable for an ETF to trade at a premium or a discount to its actual worth. To settle their holdings, most investors simply sell their ETFs to other investors on the open market. However, it is likely to amass enough ETFs to redeem them for one creation unit and then redeem the creation unit for the underlying securities. As of the large number of shares involved, individual investors rarely use this option. [3]

**The performance of top 10 ETFs as on Feb 28,2018 is here in below table:**

**Performance of ETFs [4]**

| **Schemes** | **Latest Price** | **% Change** | **Asset Size** | **NAV** | **Returns in %** (as on Aug 03, 2018) | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | (Rs. cr.) | (Rs/- Unit) | **1wk** | **1mth** | **3mth** | **6mth** | **1yr** | **2yr** | **3yr** |

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| | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Motilal MOSt Oswal NASDAQ 100 ETF | 579.00 | 0.00 | 80.84 | 486.44 | -3.6 | 3.1 | 11.5 | 12.3 | 30.5 | 24.2 | 18.4 |
| Reliance ETF NV20 | 545.59 | 0.48 | 11.73 | 540.05 | 2.1 | 7.6 | 9.3 | 7.2 | 19.8 | 19.4 | 12.0 |
| Kotak NV 20 ETF | 54.40 | 0.42 | 2.92 | 53.92 | 2.1 | 7.6 | 9.4 | 7.2 | 19.7 | 19.5 | -- |
| ICICI Prudential NV20 ETF | | - | 9.60 | 52.89 | 2.1 | 7.4 | 9.1 | 6.9 | 19.3 | 19.0 | -- |
| Edelweiss ETF - NQ30 | | - | 2.24 | 284.28 | 1.4 | 4.6 | 6.0 | 8.5 | 18.9 | 12.1 | -- |
| Reliance ETF Consumption | 54.71 | -0.18 | 15.06 | 54.67 | 1.9 | 4.2 | 3.4 | 7.0 | 17.1 | 16.5 | 13.5 |
| LIC MF ETF - Sensex | | - | 352.72 | 384.71 | 0.5 | 5.6 | 6.4 | 6.8 | 15.7 | 16.6 | -- |
| HDFC Sensex ETF | 3,891.84 | 1.42 | 31.85 | 3,853.98 | 0.5 | 5.6 | 6.3 | 6.8 | 15.7 | 16.6 | -- |
| UTI Sensex Exchange Traded Fund | 391.10 | 1.83 | 2,721.47 | 385.98 | 0.5 | 5.6 | 6.3 | 6.8 | 15.7 | 16.7 | -- |
| Reliance ETF Sensex | 384.58 | 0.00 | 24.96 | 390.72 | 0.5 | 5.6 | 6.3 | 6.8 | 15.6 | 16.6 | 11.1 |

***Benefits of ETFs:***

1. Retail, Institutional, long-term, short-term all type of investors can use the ETF according to their interest.
2. Unlike mutual funds long-term investors does not suffer any loss due to entry or exit of short-term investors.
3. The trader can also invest in intra-day trading.
4. Best for retail investors due to diversified but simple structure, less cost and small ticket size.
5. These are less expensive for big investors and arbitragers.
6. These can be traded through broker or dealer, because these are listed, like shares.
7. Investors can also buy ETFs directly from mutual fund company, advisor or trading member.
8. ETFs are traded at different rates whole day. [2]

***Some Examples of Widely Traded ETFs:***

One of the most extensively known and traded ETFs tracks the S&P 500 Index, and is named as the Spider (SPDR), and trades under the ticker SPY.

The IWM traces the Russell 2000 Index.

The QQQ tracks the NASDAQ 100, and the DIA tracks the Dow Jones Industrial Average.

Sector ETFs tracks individual industries such as oil companies, energy companies, financial companies, REITs, the biotech sector, and so on.

Commodity ETFs exist to track commodity prices including crude oil, gold, silver, and natural gas among others.

ETFs that track foreign stock market indices exist for most advanced and many evolving markets, as well as other ETFs that track currency movements globally. [5]

## III. CONCLUSION

Though Exchange Traded funds are innovated in 1989 but it took time of a decade to make existence in India. Since ETFs are in infant stage, they are not much popular. ETFs are traded on stock exchanges and easily dealt by small and short- time investors. Various ETFs are available in market, like, Index ETFs, Bond ETFs, commodity ETFs etc. Though ETFs gain wider recognition in India still investor awareness is required to make them more popular. In India ETFs are Traded on NSE.

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