Evolution of Exchange Traded Funds (ETFs) – Comparison U.S. and Indian Bourses

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Bourses across the world have endeavored to satisfy the varying risk appetites of investors through innovations undertaken in the existing financial products. Exchange traded funds (ETFs) have debut the stock markets as close competitors to both open-ended funds as well as close-ended funds. The present paper attempts to provide an insight into the mutual fund industry of the world's two major economies, one representing the developed nations i.e. U.S. and the other symbolizing the developing nations i.e. India. The ETF industry in the two countries is found to differ on account of number of ETFs active in the respective countries, resources mobilized as well as the types of investors participating in the relatively new industry. ETFs are found to have strengthened their roots in the U.S. economy whereas they are yet required to undergo a long journey before they could gain momentum in India. The study will be beneficial for the research and investment community keen at understanding the evolution and growth of exchange traded funds.

Keywords: *Evolution, Exchange-traded funds, Index funds, India, Mutual funds, U.S.*

INTRODUCTION

Exchange traded funds (ETFs) symbolize a new investment avenue that aim to provide investors with the dual advantages of diversifying their portfolio through investment in a ingle security while simultaneously enabling real time trading which, however, were not available in case of traditional mutual fund trading. ETFs had their foundation laid in open-ended and close-ended mutual funds. Hence, an insight into the mutual fund industry is essential to understand the evolution of Exchange Traded Funds (ETFs). The present study studies the antecedents of ETFs that evolved over a period of time to form the present structure of ETFs. The paper lays emphasis on the origin, growth and development of ETFs in US that holds the credit of providing the world with its first-ever ETF i.e. SPDR and extends the same to India which accounts for one of the fastest growing economies of the world.

SOURCES OF QUANTITATIVE INFORMATION

Since the present study attempts to provide a brief view of the US and Indian ETF industry and its growth over time, reports by various investment institutions such asBlackrock, ETFGI(for the US market), AMFI (Association of Mutual Funds of India), SEBI (Securities and Exchange Board of India) (for the Indian market) and respective AMCs (Asset Management Companies) (of both the

markets) till 2015 have been studied. The sources include ETP Landscape- industry highlights (Blackrock), ETFGI monthlynews letters (ETFGI) and annual reports of SEBI besides the abstracts obtained from the websites of AMFI and respective AMCs.

EVOLUTION OF MUTUAL FUND INDUSTRY

The mutual fund industry owes its existence to a Dutch merchant and broker Abraham van Ketwich who invited people to collectively pool their savings to form an investment trust named “EendragtMaaktMagt” meaning “Unity Creates Strength” in 1774. The trust provided small investors an opportunity to invest in profitable avenues and hedge risk through diversification (Rouwenhorst, 2004). The trust was a huge success in Netherlands and survived for about 120 years but was finally dissolved in 1893 (Ferri, 2007).

United States (U.S.) had its first investment trust formed in 1893 named “Boston Personal Property” which was the first close-ended fund that traded on the U.S. stock exchange (Lofton, 2007). Since these funds restricted the ability to create or redeem underlying shares, they started trading at excessive premiums or discounts to their net asset value (NAV) which made them unpopular among the investment community (Davidson, 2012). Thereafter, the formation of the “Alexander Fund” in Philadelphia in 1907 paved way for the development of open-ended mutual fund that allowed the creation and redemption of shares at regular intervals. However, the “Massachusetts Investors Trust (MIT)”, formed in 1924, holds the privilege of being the first true U.S. mutual fund that is designed in accordance with today's open-end structure (Ferri, 2007). The U.S. mutual fund industry witnessed peaks and valleys for the next few years and with the establishment of the Investment Act of 1940, the count of mutual funds increased substantially in the next few decades (Lofton, 2007).

Up to 1970, the mutual fund industry followed active management and tried to outperform the market through active selection of stocks. Owing to the high expense ratio, rapid stock turnover and difficulties encountered while forecasting market trends, mutual funds failed to provide returns superior to those of the market (Wiandt and McClatchy, 2002; Lofton, 2007). The investment community, thus, started calling for a passively managed fund that could provide returns similar to those of a stock index at minimum cost (Ferri, 2002; Lofton, 2007). Also, Eugene Fama in his paper on efficient market hypothesis further proposed that the markets are efficient enough to reflect all the available information and hence, any endeavor to beat the market wisdom will be futile (Wiandt and McClatchy, 2002). Wells Fargo Bank developed the first index fund in 1971 that aimed to replicate the returns of all the stocks comprising the New York Stock Exchange but the idea could not succeed owing to the huge expenses incurred while executing strategies associated with the fund management (Ferri, 2002). John Bogle and Dr. Burton Malkiel introduced the first commercially successful index fund titled Vanguard 500 Index Fund in 1976 that comprised of stocks included in the S&P 500 index (Lofton, 2007). However, it was only after 1986 that the fund got wide acceptance from the investment community (Ferri, 2002). In addition, the index fund industry in U.S. gained impetus only from the year 1996 (IISP Ltd., 2013).

ORIGIN OF EXCHANGE TRADED FUNDS (THE U.S. SCENARIO)

With investors now tracking the market indexes through holding a basket of securities, only one step remained for Exchange Traded Funds (ETFs) to enter the market place (Wiandt and McClatchy, 2002). ETFs already had their genes laid in the program trading or portfolio trading that revolutionized the notion “trading” in late 70s and early 80s (Gastineau, 2001). Program trading allowed the trading of a "basket of securities" like those in an index, as against the trading of an individual security, through the execution of a single order placed at the stock exchange (Carlson, 2006). The simultaneous evolution of S&P 500 index futures enabled large institutional investors to utilize program trading to hedge their positions through portfolio insurance, indulge in index arbitrage activities and pursue their other hedging objectives (Furbush, 2002). As such, institutional investors started exploiting the strategy aggressively in both cash and futures markets in order to protect their respective interests. All these developments aroused interest among the small institutions and retail investors for a portfolio that could be traded easily in the market without incurring any substantial cost (Gastineau, 2001). Although futures and program trading were the best available investment options at that time, they failed to cater to the needs of small and retail investors who found them complex and expensive (Wiandt and McClatchy, 2002).

Set against this background were the Cash Index Participations (CIPs) which were introduced in 1989 on the Philadelphia Stock Exchange. These were followed by the introduction of Index Participation Shares (IPS) on the American Stock Exchange. The market showed a great degree of enthusiasm in the new financial products. Both these instruments possessed much of the characteristics of futures than the ETFs of today since like future contracts, there was a short for every long and vice-a-versa (Wiandt and McClatchy, 2002). As such, the Chicago Mercantile Exchange (CME) and the Commodity Futures Trading Commission (CFTC) filed a suit against the Securities Exchange Commission (SEC), who had allowed the trading of such products, claiming that these products should trade on a futures market and not on a cash market. Ultimately, the SEC lost the case to CME and CFTC and stock markets were directed to close down the products (Gastineau, 2001).

At the same time, the U.S. Securities and Exchange Commission (SEC), on the request of Leland, O'Brien and Rubinstein (LOR) was making efforts to make way for the creation of a new exchange traded product that could provide institutional and retail investors with an easy way to hedge their positions. As such, the Investment Company Act Release No. 17809 was passed in 1990 that resulted in the formation of a new investment vehicle called SuperTrust. These advancements were in response to the stock market crash of 1987, a glimpse of which has been provided in the box. The structure of SuperTrust was similar to that of index fund which enabled institutional investors to trade an entire portfolio consisting of S&P 500 stocks in a single trade (Ferri, 2007). The new investment vehicle combined the characteristics of both open-end and closed-end funds. It allowed the creation and redemption of units like open-end funds and enabled intraday trading similar to closed-end funds. If the units were found to trade at a discount to their NAVs, institutional investors would step-in to arbitrage the situation. They would buy the underpriced units and at the same time sell the underlying the securities in the unit. The units would then be delivered to the fund manager who will in turn issue the underlying securities to the institutional investors. The securities would then be used to cover up the short position in the securities sold earlier. This arbitrage mechanism allowed institutional investors to lock in a risk-free profit. The procedure was reversed in case the units were found to trade at a premium. The creation and redemption process of SuperUnits helped to overcome the issues of discount and premium that were prevalent in closed-end funds (Ferri, 2002).

Owing to the regulatory delays observed in the completion of the process, the "SuperTrust" was finally launched in December 1992. The trust was formed with a maturity of 3 years and the idea was to replace the maturing units in 1995 but the replacement could not occur since it failed to attract the small and retail investors who found it to be

complex, expensive and bearing only institutional appeal (Ferri, 2007).

The American Stock Exchange (AMEX) was quick enough to take advantage of the SuperTrust Act of 1992 and filed a petition with the SEC to grant approval for the creation of the first ETF named Standards and Poor's Depository Receipts (SPDRs), popularly known as spiders(Ferri, 2002). Spiders, managed by State Street Global Advisors (SSGA), started trading at AMEX in January 1993 (Ferri, 2007). The structure of SPDRs is relatively simple and comprises of all the S&P 500 stocks, the proportion of which can be adjusted in accordance with the changes in the underlying index (Gatineau, 2001). Each unit of the SPDRs is valued at 1/10th of the value of the underlying index (Ferri, 2002). Any discrepancy observed in the market value of spiders and the stocks in the underlying index is corrected though an arbitrage process described in case of SuperUnits. The arbitrage is repeated until the deviation in prices is eliminated to such an extent that there is no profit opportunity left from such an arbitrage. SPDRs recorded an immediate success (Ferri, 2007). Ferri (2002) cites that the affordability offered by spiders to retail investors as one reason for the success of spiders over SuperUnits. The author further states that the low cost spiders had such a wide investor appeal that they stood in close competition to Vanguard 500 Index Fund.

The success story of SPDR prompted many other global players such as Morgan Stanley, Barclays Global Investors and Vanguard to enter the industry with a new generation of ETFs that aimed to replicate the performance characteristics of varied asset classes such as sector-specific ETFs, country ETFs, commodity ETFs, currency ETFs and many more (Ferri, 2002, 2007).

Since 2006, the U.S. ETF industry has grown tremendously with the number of ETFs increasing from 350 in 2006 to 1,259 ETFs in 2013. The assets under ETFs increased simultaneously from U.S. $ 416 billion to U.S. $ 1,614 billion in 2013. Presently, the industry comprises of a wide variety of ETFs such as actively managed ETFs, fixed income ETFs, global emerging market ETFs, leveraged ETFs and so on. As on 31 March 2015, the U.S. ETF industry comprised of 1,405 ETFs from 59 providers with assets under management of around U.S. $ 2007 billion, listed at the three stock exchanges of the U.S. (ETFGI, 2015).

THE INDIAN SAGA

The year 2014-15 witnessed an increased investor confidence in the financial stability of the Indian capital markets on account of strong fundamentals and growth prospects reported for the Indian economy. During the year 2014-15, Indian ETFs listed abroad such as the WisdomTree India Earnings Fund, iShares India 50 ETFand PowerShares India Portfolio recorded a gain of 27%, 26.4% and 26.7% respectivelyagainst the 4.8% gain recorded for iShares MSCI Emerging Markets ETF (Lydon, 2015).Hence, the following section proceeds to discuss the budding ETF sector in the Indian mutual fund industry.

The mutual fund industry in India evolved with the establishment of the Unit Trust of India (UTI) in 1963 as a joint effort on the part of the Government of India and the Reserve Bank of India (AMFI, 2014). UTI Mutual Fund launched its first open-end scheme named US64 in 1964 which was accredited with a huge success (Singh, 2003). This era marked the beginning of the first phase of mutual fund industry from the year 1964 to 1987. The second phase of the mutual fund industry (1987-1993) broke the monopoly of the UTI with the entry of various public sector mutual funds managed by public sector banks, Life Insurance Corporation (LIC) of India and General Insurance Corporation (GIC) of India (AMFI, 2014). State Bank of India (SBI) launched the first non-UTI mutual fund named SBI Mutual Fund in 1987. Canbank Mutual Fund (December 1987), Punjab National Bank Mutual Fund (August 1989), Indian Bank Mutual Fund

(November 1989), LIC Mutual Fund (June, 1989), Bank of India (June 90), GIC Mutual Fund (December, 1990) Bank of Baroda Mutual Fund (October 1992) were some of the other schemes that followed the pursuit (Kapil, 2011). With the liberalization of the financial sector in 1993, the mutual fund industry entered its third phase of growth that led to the entry of private sector players in the industry. The year 1993 was also marked by the introduction of mutual fund regulations that required all the mutual funds to be registered with the Securities Exchange Board of India (SEBI, 2013). These guidelines were later revised and replaced by the SEBI (Mutual Fund) Regulations 1996. In view of the mushrooming growth of the mutual fund industry, Association of Mutual Funds in India (AMFI) was set up in 1993 in order to ensure ethical code of conduct and protect investors' interests. The UTI reigned the industry till 1994-95 with around 76% of the resources being mobilized by the trust. However, a shift was observed in the year 1995-96 when the trust repurchased its large number of units, thus, providing an opportunity to the private sector players to grow and expand. As a result, the year 1999-2000 witnessed a sharp transposition in the industry when out of the total funds mobilized, private sector funds (with around 120 schemes offered to the investors) contributed 78.15% share to the total funds mobilized (Machiraju, 2010). The bifurcation of the UTI into Specified Undertaking of the UTI (governed by the Government of India) and UTI Mutual Fund (governed by the Mutual Fund Regulations) in 2003 led to the beginning of the fourth phase of the mutual fund industry. As of today, the industry is heralding towards a new era of consolidation with a number of mergers and acquisitions taking place among the private players (AMFI, 2014). As on 31 March 2005, the industry comprised of 29 mutual funds with eight in the public sector and twenty one in the private sector (Machiraju, 2010).With regard to the present scenario, out of Rs. 1,10,86,260 crores (gross) funds mobilized during the year 2014-15, Rs. 91,43,962 crores were mobilized by private sector mutual funds and Rs. 19,42,297 crores by public sector mutual funds (SEBI, 2015). Hence, private sector was found to continue to lead the mutual fund industry with 82.48% of the resources being mobilized by the private players.

Initially, open-ended schemes were more popular in India compared to the close-ended schemes which failed to attract the Indian investors during the early years of their inception. However, the scenario changed in 2006 when SEBI prohibited open-ended funds to amortize their initial expenses incurred at the time of initiating a new fund offer. This announcement made close-ended funds more appealing to the mutual fund houses who believed that the lock-in period involved in case of close-ended funds would restrict pre-mature withdrawals by investors which, in turn, would help them earn returns higher than those of the open-ended funds on account of the stable corpus of resources available with the fund (Adajania, 2010). As such, the number of close-ended schemes increased considerably from 47 in 2004-05 to 129 in 2005-06 and then further to 364 in 2007-08 (SEBI, 2005, 2006 and 2008). On 31 March 2015, there were 1,884 mutual fund schemes operating in the country out of which 810 (42.99%) comprised of open-ended schemes, 1002 (53.18%) comprised of close-ended schemes and 72 (3.82%) of interval schemes (SEBI, 2015).

The growing sophistication of the world equity markets and tremendous growth observed in the mutual fund industry made it difficult for the fund managers to outperform the market consistently. As such, managers started buying stocks, either deliberately or accidentally, similar to those comprising the market index. This led to the development of passive investment strategy that allowed control over the cost and risk associated with the portfolio (IISP Ltd., 2013). As a result, index funds were formed with Principal Index Fund being the first index fund to be launched in India in 1999. The fund is designed to track the performance of

CNX Nifty. The next index fund to enter the industry was UTI Nifty Index Fund in 2000. The race was followed by Franklin India Index Fund (June, 2000), SBI Nifty Index Fund (Dec, 2001), ICICI Prudential Index Fund (Feb, 2001), HDFC Index Fund (Jul, 2002), Birla Sun Life Index Fund (Sep, 2002), LIC NOMURA MF Index Fund (Nov, 2002), Tata Index Fund (Feb, 2003), Canara Robeco Nifty Index Fund (Sep, 2004), IDFC Nifty Fund (May, 2010), Taurus Nifty index Fund (Jun, 2010), IDBI Nifty Index Fund (Jun, 2010) and Reliance Index Fund (Sep, 2010). All these funds are designed to replicate the risk-return characteristics of the CNX Nifty index. Goldman Sachs Asset Management (India) Private Limited launched its first index fund named Goldman Sachs CNX 500 Fund in Nov 2008 that consisted of stocks comprising the CNX 500 index. ICICI Prudential Asset Management Company and IDBI Asset Management Company launched their own respective index funds in June 2010 and September 2010 respectively that tracked the performance of CNX Nifty Junior index. IIFL Dividend Opportunities Index Fund (Jun, 2010) and Principal Index Fund (May, 2014) were the next index funds to enter the industry that aimed to follow the CNX Dividend Opportunities and CNX Midcap Index respectively.

The rationale behind the introduction of exchange traded funds (ETFs) in the Indian market is not far different than that of the U.S. market. The inflexibility of intra-day redemption associated with open-ended funds and the tendency of close-ended funds to trade at excessive premiums or discount aroused the need for a readily tradable exchange traded vehicle that could be traded throughout the day and the market value of which does not deviate significantly from that of its underlying portfolio (or asset).

In India, Benchmark Asset Management Company Pvt. Ltd. (taken over by Goldman Sachs Asset Management Company in 2011) launched the first ETF named Nifty BeES on the National Stock Exchange (NSE) in December 2001. The fund is promoted as a hybrid security combining the advantages of both open-ended and close-ended funds. It allowed investors to gain exposure to S&P CNX Nifty Index through the trading of a single security listed on the stock exchange. It is priced at 1/10th of the value of the index and is traded on the capital market segment of the stock exchange. The in-kind creation and redemption feature of the fund allowed authorized participants to exploit any mispricing observed between the market price and Net Asset Value (NAV) of the fund (Nifty BeES: India's first ETF launched, 2001). The fund was not an immediate success. It took a couple of years for the fund to gain momentum and today the fund accounts for the largest fund among the available ETFs with assets under management (AUM) reported to be Rs. 888.93 crores as on 31 March 2015 (Goldman Sachs, 2015).

Benchmark mutual fund house came out with its next schemes titled Junior BeES and Bank BeES in 2003 and 2004 that aimed to provide exposure to risk-return characteristics of stocks comprising the CNX Nifty Junior and CNX Bank Index respectively. Each unit of Junior BeES is priced at 1/100th of the CNX Nifty Junior index and each unit of Bank BeES is priced at 1/10th of the value of the CNX Bank index. ICICI prudential mutual fund came out with the first ETFnamed SENSEX Prudential ICICI Exchange Traded Fund (i.e. SPIcE) to be traded on Bombay Stock Exchange (BSE)in 2003 which was designed to track the value of 1/100th of the SENSEX. Unit Trust of India also joined the quest with its first ETF titled UTI Sunder launched in 2003 (Pathak, 2010). However, the fund was merged with UTI Nifty Index Fund on 15 March 2012 and at present, the fund aims to replicate the performance of CNX Nifty index. Thereafter, a number of new schemes entered the industry. A brief view of the various equity ETFs available in India is given in Table I.

Table 1: Profile of Equity ETFs available in India as on 31 March 2015

S. No.	Fund Name	Symbol	Launch Date	Benchmark Index	Fund House
1.	Goldman Sachs Nifty Exchange Traded Scheme	NIFTYBEES	Dec 28, 2001	CNX Nifty	Goldman Sachs Mutual Fund
2.	Goldman Sachs Nifty Junior Exchange Traded Scheme	JUNIORBEES	Feb 21, 2003	CNX Nifty Junior	Goldman Sachs Mutual Fund
3.	ICICI Prudential SPIcE Fund	ISENSEX/SPICE	Jan 10, 2003	S&P BSE Sensex	ICICI Prudential Fund House
4.	Goldman Sachs Banking Index Exchange Traded Scheme	BANKBEES	May 27, 2004	CNX Bank	Goldman Sachs Mutual Fund
5.	Goldman Sachs PSU Bank Exchange Traded Scheme	PSUBNKBEES	Oct 25, 2007	CNX PSU Bank	Goldman Sachs Mutual Fund
6.	Kotak PSU Bank ETF	KOTAKPSUBK	Nov 8, 2007	CNX PSU Bank	Kotak Mahindra Mutual Fund
7.	Kotak Sensex ETF	KTKSENSEX	June 6, 2008	S&P BSE Sensex	Kotak Mahindra Mutual Fund
8.	R*Shares Banking Exchange Traded Fund	RELBANK	June 19, 2008	CNX Bank	Reliance Mutual Fund
9.	Quantum Index Fund	QNIFTY	July 10, 2008	CNX Nifty	Quantum Mutual Fund
10.	Goldman Sachs S&P CNX Shariah Exchange Traded Scheme	SHARIABEES	March 18, 2009	CNX Nifty Shariah	Goldman Sachs Mutual Fund
11.	Kotak Nifty Exchange Traded Scheme	KOTAKNIFTY	Feb 8, 2010	CNX Nifty	Kotak Mahindra Mutual Fund
12.	MoSt Shares M50	M50	July 28, 2010	CNX Nifty	MotilalOswal Mutual Fund
13.	Goldman Sachs Infrastructure Exchange Traded Scheme	INFRABEES	Sep 29, 2010	CNX Infrastructure	Goldman Sachs Mutual Fund
14.	MoSt Shares M100	M100	Jan 31, 2011	CNX Midcap	MotilalOswal Mutual Fund
15.	Religare Invesco Nifty Exchange Traded Fund	RELGRNIFTY	June 6, 2011	CNX Nifty	Religare Invesco Mutual Fund
16.	Birla Sun Life Nifty Exchange Traded Fund	BSLNIFTY	July 22, 2011	CNX Nifty	Birla Sun Life Mutual Fund
17.	India Infoline Nifty Exchange Traded Fund	IIFLNIFTY	Oct 18, 2011	CNX Nifty	India Infoline Mutual Fund
18.	SBI SENSEX ETF	SBISENSEX	March 8, 2013	S&P BSE Sensex	State Bank of India Mutual Fund
19.	R*Shares CNX 100 Fund	RELCNX100	March 22, 2013	CNX 100	Reliance Mutual Fund
20.	ICICI Prudential Nifty ETF-Growth	INIFTY	March 20, 2013	CNX Nifty	ICICI Prudential Mutual Fund
21.	ICICI Prudential CNX 100 ETF-Growth	ICCNX100	Aug 20, 2013	CNX 100	ICICI Prudential Mutual Fund
22.	R*Shares Nifty Exchange Traded Scheme	RELNIFTY	Nov 22, 2013	CNX Nifty	Reliance Mutual Fund
23.	R*Shares Consumption Exchange Traded Fund	RELCONS	Mar 28, 2014	CNX Consumption Index	Reliance Mutual Fund
24.	Goldman Sachs Mutual Fund- CPSE Exchange Traded Scheme	CPSEETF	March 28, 2014	CPSE Index	Goldman Sachs Mutual Fund
25.	R*Shares Dividend Opportunities ETF	RELDIVOPP	April 7, 2014	CNX Dividend Opportunities	Reliance Mutual Fund
26.	Kotak Banking Exchange Traded Fund	KOTAKBKETF	Nov 28, 2014	CNX Bank	Kotak Mahindra Mutual Fund
27.	R*Shares Dividend Opportunities ETF	RELDIVOPP	April 7, 2014	CNX Dividend Opportunities	Reliance Mutual Fund
28.	Kotak Banking Exchange Traded Fund	KOTAKBKETF	Nov 28, 2014	CNX Bank	Kotak Mahindra Mutual Fund
29.	SBI ETF Nifty Junior Fund	SETFNIFJR	Mar 16, 2015	CNX Nifty Junior	SBI Mutual Fund
30.	SBI ETF Banking Fund	SETFBANK	Mar 16, 2015	Bank Nifty	SBI Mutual Fund

(Compiled from: NSE, Moneycontrol, Valueresearchonline)

In 2014, the Government of India (GOI) conceived the idea of ETFs as a tool to disinvest a portion of its holding in Public Sector Units (PSUs). Goldman Sachs Asset Management (India) Pvt. Ltd. was given the responsibility of managing such a fund and as such, the fund house came out with Central Public Sector Enterprises Exchange Traded Fund (CPSE ETF) in March 2014 with the aim to provide returns similar to those of the CPSE index. The fund proved to be a great success since it enabled government to harvest Rs. 3000 crores through the disinvestment process undertaken by this route (Palande, 2014).

The notion of commodity ETFs was first introduced in the world in May 2001 in India when Benchmark Asset Management Company filed its prospectus with SEBI with regard to the introduction of gold ETFs. However, the idea could materialize only in 2007 after certain regulatory restrictions were imposed. Gold BeES was the first ETF to be launched in India in 2007 by Benchmark mutual fund house (Benchmark, 2009). Thereafter, a number of schemes such as Goldshare (Mar, 2007), Kotakgold (Jul, 2007), Relgold (Nov, 2007), Qgoldhalf (Feb, 2008), Sbigets (April, 2009), Religarego (March, 2010), Hdfcmfgetf (Aug, 2010), Igold (Aug, 2010), Axisgold (Nov. 2010), Bslgoldetf (May, 2011), Idbigold (Nov, 2011), Crmfgetf (March, 2012) and Mgold (Mar, 2012) were launched in India that were designed to track the real-time price of gold. Each unit of these gold ETFs, except for Qgoldhalf, is priced at approximately one gram of the price of gold. Qgoldhalf tracks the price of approximately half gram of gold. All these schemes are statutorily required to pool all their resources in gold and gold related instruments (Pathak, 2010).

India holds the privilege of being the first country to design an ETF that caters to the needs of risk-averse investors who wish to invest their funds in risk-free securities. Liquid BeES is the first money market ETF launched in India in 2003 by Goldman Sachs Asset Management Company. The funds gathered through Liquid BeES are invested in short-term debt and money market securities (Benchmark, 2009). Later on, in 2014, LIC Nomura Mutual Fund launched the G-Sec Long Term Exchange Traded Fund that comprised of the securities held by GSEC 10 NSE Index. The fund is the second of its type in the money market ETF category.

Catering to the advantages that international investment adds to an investor's portfolio, international ETFs were launched in India in 2010.The investment domain of international ETFs is the stocks that are domiciled in other countries. Goldman Sachs Asset Management (India) Pvt. Ltd. launched the first international ETF in India in March 2010 and named it Hang Seng BeES. The fund aims to provide returns corresponding to those of Hang Seng Index, the index that serves as the economic barometer of Hong Kong. This was followed by the launch of N100 in March 2011 by MotilalOswal mutual fund house that invests in stocks that form part of the Nasdaq 100 of U.S.

India also has its presence felt in the global ETF industry through some of its exchange traded products listed at the international financial markets. India is seen as one of the most vital emerging economies in the world on account of its huge population and growth prospects. The Indian ETFs listed in U.S. are MSCI India Index Fund (INDA), India Earnings Fund (EPI), S&P India Nifty Fifty Index Fund (INDY), India Portfolio (PIN), MSCI India Index ETN (INP), India Small-Cap Index ETF (SCIF), Daily India Bulls 2x Shares (INDL), India Consumer ETF (INCO), India Infrastructure ETF (INXX), MSCI India Small Cap Index Fund (SMIN) and India Small Cap ETF (SCIN). Among the available ETFs, MSCI India Index Fund (INDA) accounts for the largest and the most popular ETF in U.S. (ETFdb, 2015).

During the financial year 2015, out of the 1,638 mutual fund schemes operating in the country, 1346 accounted for income/debt oriented schemes, 434 accounted for growth/equity oriented schemes, 25 for balanced schemes, 48 for exchange traded schemes and 31 for fund of funds investing overseas.

With regard to the funds mobilized during the period, the mutual fund industry had Rs. 10,82,757 crores of assets under management (AUM) out of which 64.11% comprised of income/debt oriented schemes, 31.87% comprised of growth/income oriented schemes, 2.43% of balanced schemes, 1.36% of exchange traded schemes and 0.22% of fund of funds investing overseas (SEBI, 2015). In view of the fact that ETFs account for only 1.6% of the total funds mobilized by the mutual fund industry, ETFs have a long voyage to undertake before they could taste success in India.

U.S. VS INDIA

The above discussion provides a glimpse of the mutual fund industry of both U.S. and India with special reference to the ETF segment. The two industries exhibit a large variation in terms of their origin and operational characteristics. The U.S. investors have already embraced the concept of exchange traded funds as reflected in the number of ETFs active in the country (1405 as on 31st March 2015) and assets managed by the ETF industry (US$ 2007 billion as on 31st March 2015). On the other hand, the investors in India are still reluctant to adopt the new investment idea. As on 31 March 2015, there are 45 ETFs listed with the two stock exchanges of India (i.e. NSE and BSE) with assets under management amounting to Rs. 14715 crores. The various myths surrounding ETFs with respect to their structure, liquidity, cost-effectiveness etc. have held them back from becoming popular in the country. While the U.S. ETF industry has witnessed an increasing participation on the part of both retail and institutional investors over the past few years, the Indian industry continues to be dominated by the corporate houses and institutional investors. Although a significant increase has been observed in the amount of resources invested by retail investors i.e. from Rs. 233.19 crore in 2008-09 to Rs. 3094.48 crore in 2014-15, the giant corporate houses and big financial institutions continue to be the major players in the Indian ETF industry. The U.S. industry has evolved over a period of time with a lot of innovation taking place in the ETF market. The industry has witnessed an increase in the variety of ETFs available ranging from those tracking a particular index or sector of the home country to those tracking the specific sectors of another country. There are ETFs that provide exposure to the dynamics of an emerging economy to those that are based on theme investing (that covers the area of clean energy, social responsibility etc.), leveraged investing (that aims to provide returns twice or thrice than that of the market index) and short investing (that aims to provide returns opposite to that of the market). Leveraged and short ETFs are much popular among the hedge fund community since they enable them to implement their mega bets in either direction in the most convenient way. However, the industry in India is much at a nascent stage with the total number of ETFs categorized into four different categories i.e. equity ETFs, gold ETFs, fixed income (or debt) ETFs and ETFs tracking international indices. Owing to the cultural preferences and the love that Indians attach to the yellow metal, Indian investors are more inclined towards gold ETFs compared to equity ETFs which came much earlier than the former. The country has only two ETFs i.e. Hang Seng BeES and N100 that are designed to trace the returns of Hang Seng Index and Nasdaq 100 respectively. The lack of awareness about the new exchange traded vehicle among the investment community has also hindered the progress of ETFs in the country. In addition, the conventional fund managers are still cautious to embrace the new idea. They fear the changes that their present business structures would have to undergo in case they adopt the new exchange traded vehicle. Although the reasons underlying the introduction of exchange traded products in both the countries remain more or less the same, the industry in India is much narrow compared to that of the U.S. and has a long way to evolve before it could compete with the world's major powers.

CONCLUSION

During the last few years, the global ETF industry has seen a tremendous growth in both the number and wealth invested in ETFs. As on 31 March 2015, the global ETP industry comprised of 5497 ETPs with assets under management of around U.S. $ 2933 billion and iShares acquiring the top position followed by Vanguard and State Street Global Advisors. U.S. occupies a pivotal position in the global ETP industry with U.S. $ 2097.3 billion being mobilized by the U.S. ETP industry alone (Blackrock, 2015). The present paper attempts to understand the evolution of one of the fastest growing segment of the mutual fund industry i.e. exchange traded funds (ETFs) in U.S. and India. The paper provides a glimpse of the various antecedents of exchange traded products that evolved over a period of time and brought about changes in the underlying structure of ETFs that gave rise to the currently traded ETFs. The paper also reviews the stock market crash of 1987 which aroused the need for the development of such an exchange traded vehicle that could provide immediate liquidity. The paper then focuses attention on the variety of ETFs offered in the two countries, the amount of resources mobilized by the funds and the types of participants in the market that set the two countries apart from each other. On the basis of discussion and statistics stated in the present study, the U.S. ETF industry is found to be much more flourished than that of the Indian ETF industry. The various myths surrounding the exchange traded funds, reluctance on the part of fund managers to embrace the new concept and lack of awareness among the investment community about the new investment avenue have held back the ETFs from becoming popular in India.

Owing to the special features inherent in the exchange traded funds,the industry holds the potential to grow by leaps and bounds in the near future. The convenience in investment, market traced returns, cost effectiveness combined with massive liquidity can make ETFs an irresistible product for a varied class of investors. ETFs enable retail and small investors to diversify their portfolio through a single investment vehicle and to change their position (long or short) as and when desired at any time of the day. ETFs enable large institutional investors such as Foreign Institutional Investors and Financial Institutions (like banks, mutual funds, pension funds and insurance companies) to easily allocate their investment resources without being affected by the implicit cost incurred in the form of cash drag. As regards active managers, ETFs offer them an opportunity to equitize their cash without sacrificing liquidity. Internationally, ETFs have occupied a prominent place in the portfolios of hedge fund managers who find them as an attractive investment option for executing their hedging strategies. With ETFs tracking a wide variety of asset classes such as equity, fixed income, commodity, real estate, currency and so on, it has become easy for both retail and institutional investors to gain exposure to a variety of asset classes which was difficult a few years back. There is no doubt that ETFs have made their presence felt in the global mutual fund industry and are likely to gain momentum in the forthcoming future.

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