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Mutual Funds and Exchange Traded Funds in India: A Comparative Analysis

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ABSTRACT

Indian financial markets are rapidly progressing and offering alternative investment avenues to mobilize household savings into productive investments. Mutual funds and exchange-traded funds have emerged as important investment instruments providing benefits of portfolio diversification, professional expertise, high returns and liquidity. However, these funds have their own features, management criteria, cost structure, as well as risk and return profile. The present study focuses on the comparative analysis of both these funds to facilitate investors in making informed investment decisions in these funds. The study is mainly secondary data based. The paper highlights the types and composition of both funds, a comparison over different aspects and challenges faced in the Indian context.

***Keywords**: Mutual Funds, Portfolio Diversification, Exchange Traded Funds, Financial Markets.*

Introduction

India is the fastest-growing fourth-largest economy in the world in terms of GDP. The country has significant growth potential supported by its demographic dividend, rapid technological innovation and digital transformation. The nation now has a vision to become a developed economy by the centenary year of independence. Sustainable economic growth and development depend significantly on the mobilization of savings into productive investments. Investment plays a dual role in overall economic development by expanding productive capacity and generating income as well as employment. Therefore, enhancing household participation in financial markets and promoting investment is a very important policy priority. In India, household savings are approximately 28% of the total GDP, which is one of the highest in the world (World Bank, 2012). It reveals the investment potential in the Indian financial market.

Traditionally, Indian household savings were guided by the motive of meeting unforeseen contingencies rather than the objective of earning profits. The main saving instruments were the post office savings, KisanVikasPatras, National Savings Certificates, and bank fixed deposits. These were considered safe with capital protection along with fixed returns. However, the Indian financial market has undergone rapid transformation over the past few decades. Economic reforms, the emergence of multinational companies and start-ups, technological innovations, and increasing digitalization have opened up vast investment opportunities for investors. A wide range of financial products like equities, debentures, bonds, government securities, mutual funds, exchange-traded funds (ETFs), insurance products, commodities, bullion, etc. have emerged as alternative investment instruments.

Among all these investment options, mutual funds and ETFs are gaining popularity due to their portfolio diversification benefits, professional management, and comparatively lower risks. Both these funds provide the opportunity of participating in the Indian securities market without the need to choose individual securities, thereby reducing risk through portfolio diversification. These funds offer the advantages of higher returns as well as liquidity. Along with the similarities, the funds differ significantly in composition, cost structure, risk, return and redemption aspects. Therefore, a detailed comparative study is needed to guide the investors to select a suitable fund.

Against this backdrop, the present study is a comparative analysis of both mutual funds and ETFs in India. This paper analyzes their types, composition, returns, associated risks and challenges in the Indian context. This research would be useful for investors in making informed investment decisions in mutual funds and ETFs.

Research Methodology

The study is based on secondary data. For the purpose of collecting information relating to the types of mutual funds and ETFs, their composition, return, risk and cost structure etc. different related websites have been visited. Data is collected from annual reports of different companies, Reserve Bank of India, publications of Securities and Exchange Board of India, stock exchanges, research articles, books etc. Data has been analyzed to elaborate composition, finding out returns, risks, and for making comparative analysis of mutual funds and ETFs in India.

Mutual Funds and Their Types

Mutual funds pool money from numerous investors and allocate funds among equity shares, debentures, bonds, government securities and various money market instruments. This portfolio is managed by experienced fund managers, whose prime objective is to maximize returns while minimizing risks. These fund managers periodically rebalance portfolios according to market conditions and investment objectives. For these services the Asset Management Companies (AMCs) charge annual expenses known as expense ratio, and is generally expressed as a percentage of total funds invested. Mutual funds are of different types in terms of fund composition, return and risk aspects. Major categories are equity funds, debt funds, hybrid funds, liquid funds, fund of funds, etc. Different types of mutual funds have been explained below.

- **Equity Mutual Funds**

These funds consist of stocks of different companies as per the specific nature of mutual fund. These funds generally maintain complete exposure to equity and normally do not invest in debt instruments like bonds or government securities. These are characterised as high risk and high return funds. Owing to their equity-oriented nature, there always remains a high scope of long-term capital appreciation, but with greater market risks. Therefore, these funds are more suitable for investors with long-term investment goals. Except for passive schemes such as index funds, most equity mutual funds are actively managed by the fund managers. SEBI has fixed the guidelines for the exposure of different types of funds to different types of securities, as shown in Table 1.

Table 1: Equity Mutual Funds

S. No.	Name of fund	Composition of Fund	Risk	10 Year CAGR*
1	Large cap funds	Minimum 80% investment in India's largest companies	High	15.5%
2	Mid cap funds	Minimum 65% of investment in medium-sized companies	High	20.5%
3	Small cap funds	Minimum 65% of investment in small-sized companies	Very high	22.5%
4	Flexi-cap funds	Minimum 65% of its assets in equities, but there is no fixed allocation among large-, mid-, and small-cap stocks.	High	21.0%
5	Focused funds	Limited number of stocks	High	17.2%
6	Index funds	Index funds imitate the performance of a market index, e.g., the Nifty 100 index fund will invest in the same 100 index companies with nearly the same weight age	High	14.4%
7	Thematic funds	One broad investment theme with moderate diversification	Very high	18.8%

8	Sectoral funds	Investment in one specific sector with lowest diversification. Example: Banking, Energy, IT sectors etc.	Very high	21.7%
9	Contra funds	They invest in securities or sectors that are presently unpopular or undervalued, with the expectation that they will recover and perform well in the future.	Very high	17.5%
10	Equity-linked saving scheme	Must invest minimum 80% in equities and equity-related instruments. These funds are tax-saver funds, and the money is locked in for a minimum of 3 years	Very high	20.6%
11	Multicap funds	Must invest minimum 25% in each category among large cap, mid cap, and small-cap stocks	Moderate to high	18.7%

Source: Tickertape, (2026)
**Maximum compound annual growth rate by any fund*

- **Hybrid Mutual Funds**

Hybrid mutual funds are a combination of equity shares and debt instruments such as corporate bonds and government securities. These funds achieve a balance between risk and return. Equity exposure ensures a good return, whereas the bonds and securities cover the risk. The proportion allocated to each asset class varies according to the investment mandate of the fund. In certain hybrid funds, the fund managers may invest some amount in gold and silver also. These funds enhance diversification and are expected to perform well during volatile market conditions and geopolitical uncertainties. Different types of hybrid mutual funds and their composition are shown in Table 2.

Table 2: Hybrid Mutual Funds

S. No.	Name of fund	Composition of Fund	Risk	10 years CAGR*
1	Multi asset allocation fund	Fund includes diversified investment among different assets with at least 10% of the total amount in equity, debt, and gold each	Moderate to high	19.0%
2	Balanced advantage fund	Equity or debt exposure can dynamically swing anywhere from 0% to 100%, depending on the market conditions	Moderate	13.0%
3	Aggressive hybrid fund	Allocates 65%–80% of its portfolio to equity and equity-related instruments, while the remaining 20%–35% is invested in debt instruments	Moderately high	17.0%
4	Conservative hybrid fund	75%–90% in debt and debt-related instruments, and 10%–25% in equity and equity-related instruments	Lower	10.3%
5	Equity saving fund	Minimum 65% in equity/arbitrage and at least 10% in debt	Low to moderate	10.7%
6	Arbitrage fund	Minimum 65% in equities/ derivatives. Arbitrage funds generate returns by taking advantage of temporary price differences for the same asset between different market segments	Very low	6.57%

Source: Tickertape, (2026)
**Maximum compound annual growth rate by any fund*

- **Debt Mutual Funds**

In debt funds, the investment is made in Government Securities, corporate bonds, treasury bills, etc. ensuring almost fixed returns. But the return of these types of funds is very less as compared to the equity and hybrid funds. These provide the safest mode of investment in mutual funds and are suitable over equity funds when the investment horizon is shorter. These are preferred by the investors with a low risk appetite and with short to medium-term investment duration. These funds are also suitable for senior citizens who want a constant and continuous source of income. Many of these funds are considered better investment options as compared to bank fixed deposits due to their higher rate of return. There are some liquid funds and overnight funds that are used by investors to invest money for a very short period of time. The most common debt funds are represented in Table 3.

Table 3: Debt Mutual Funds

S. No.	Name of fund	Composition of Fund	Risk	10 years CAGR*
1	Money market fund	Invest exclusively in highly secure, short-term debt instruments with a maximum maturity period of one year.	Low	6.84%
2	Corporate bond fund	**Allocation of minimum 80% of their total assets in corporate bonds with high credit ratings, generally rated AA+ and above.**	Low to moderate	7.61%
3	Floating rate fund	Minimum 65% of their total assets is invested in floating debt instruments	Low to moderate	7.79%
4	Banking and PSU fund	Invest at least 8**0% in Bank/PSU debt instruments**	Very low	7.64%
5	Liquid fund	Invest in prime, highly secure quality debt tools with a maximum maturity period of 91 days	Very low	6.38%
6	Credit risk fund	Invest in lower-rated securities at elevated interest rates	High	9.55%

Source: Tickertape, (2026)
**Maximum compound annual growth rate by any fund*

- **Fund of Funds**

This type of fund is a super fund including bucket of different other funds. In this fund investment is not made in different securities rather on different other mutual funds to get the objectives of investment diversification along with the advantage of specialized markets. But the expense ratio of these funds is generally high because investors have to bear the expenditure both at fund of fund(FoF) level and at the underlying fund level. But these funds offer some unique investment options unavailable in other funds like investment in the international equity market, investment in gold and silver and solution oriented investment like retirement and childhood planning funds etc. Common FoFs are shown in Table 4.

Table 4: Fund of Funds

S. No.	Name of fund	Composition of Fund	Risk	10 years CAGR*
1	Gold FoFs	Invests its corpus in the units of Gold ETFs. The underlying Gold ETFs strictly buy and hold physical gold bullion of 99.5% purity or higher	High	16.3%
2	Silver FoFs	Does not invest directly in physical silver. Instead, it invests primarily in units of Silver ETFs, which itself holds physical silver of high purity (typically 99.9%)	High	48.3%#
3	Domestic FoFs	It pools investors' capital to invest in the units of other mutual funds operating within India, rather than buying individual stocks or bonds directly	High	16.0%
4	FoFs (International)	P**ools Indian investors' capital to invest in the overseas mutual funds, ETFs, or venture capital funds operating outside India**	Very High	19.4%

Source: Tickertape, (2026)
**Maximum compound annual growth rate by any fund*
#CAGRof 3 years

Exchange Traded Funds and Types

Exchange Traded Funds (ETFs) are very unique and attractive investment option that is relatively newer in India. ETFs consist of a basket of stocks/securities that track a particular index, sector, commodity, or asset class. These combine the diversification benefits of mutual funds with the trading flexibility of equity shares. Unlike mutual funds, ETFs are traded on stock exchanges like ordinary shares, and during stock market hours, investors can buy or sell ETFs at the current market prices. In contrast to actively managed mutual funds, most ETFs are passively managed and aim to track the performance of a benchmark index, resulting in lower management costs and expense ratios. Similar to mutual funds, ETFsare offered by different fund houses, and the money is invested in several companies to diversify the portfolio and minimise the risk. Different exchange-traded funds track different indexes like Nifty 50 index, IT index, Bank Nifty, Nifty 500 index etc. The composition and allocation of an ETFare the same as in the index. Common ETF types are explained in Table 5.

Table 5: Common ETF Types and Their Composition

Types of ETF	Composition	10 years CAGR*	Risk Factors
Index ETFs	These ETFs follow a specific index like the Nifty 50, Nifty Midcap 150, Nifty 500, Nifty Smallcap 250, etc. Index ETF consist of the exact stocks that make up that index.	12.5%	Exposed to systemic stock market crashes with no active fund manager available to pull money into safe cash reserves during down cycles.
Sector and Thematic ETFs	These funds focus entirely on a specific industry or sector, keeping macroeconomic trends in view. The sectors may be like: banking, technology, automobiles etc., and the themes may be like: electric vehicles, green energy, artificial intelligence etc.	12.6%	Suffer from heavy concentration risk in a single industry, making them highly vulnerable to specific regulatory shifts and multi-year cyclical downturns.
Commodity ETFs	Commodity ETFs track the real-time spot prices of raw materials or physical assets. Commodity ETFs hold physical inventory. Common ETFs in this category are Gold ETFs, Silver ETFs, and other ETFs that follow Nifty Commodities Index	13.9%	Generate no ongoing cash flows or corporate dividends, with returns reduces over the time due to fees of physical storage and vault insurance.
Global /International ETFs	Global ETFs invest directly in foreign stock markets, regions, or sectors. These funds are issued by domestic asset management companies but track offshore benchmarks. They trade in Indian rupees just like domestic shares during regular Indian market hours.	21.3%	Exposed to currency volatility between the Indian and foreign currencies, along with sudden SEBI-mandated fund inflow restrictions on international assets

**Compound Annual Growth Rate*

Comparative analysis

Mutual funds and ETFs, are good investment avenues for investors to participate in the Indian financial markets. Both are very good options for retail investors with limited knowledge of the Indian stock exchange. Both these funds provide investment diversification guided by expert opinion. Despite these similarities, the funds differ in management system, trading flexibility, risk and return portfolio, cost structure, redemption mechanism, etc. Therefore, a comparative analysis of both the funds is necessary for a proper understanding of the investors. The main differences between mutual funds and ETFs are shown in Table 6.

Table 6: Comparison of Mutual Funds and ETFs

S. No.	Feature	Mutual Funds	ETFs
1	Requirement of demat and trading account	No	Yes
2	Sold through	Asset Management Company	Stock exchange
3	Role of fund manager	Active	Passive
4	Composition and allocation	Selected by the fund manager according to the type of fund	Based onthe underlying index
5	Redemption Price	At day-end NAV	Real-time pricing
6	Trading time slot	Any time	During stock exchange hours
7	Rate of Return	Generally high for actively managed funds	Nearly equal to the index return
8	Exit load	Generally, yes, if sold before a specific time (typically 1 year)	No

9	Expense Ratio	Relatively high	Relatively low
10	Liquidity Issue	No issue of liquidity	Liquidity issue in some ETFs
11	Long-term systematic investment(SIPs) and convenience	Very Convenient	Poor

Source: Own compilation

Challenges in the Indian Investment Market

As the Indian economy is in its developing phase, the Indian investment market also faces severe challenges. A large population of India is close to the poverty line, where people focus on meeting both ends, leaving little scope for savings and investment. The majority of the Indian population resides in rural areas, facing problems of poor financial literacy, limited digital awareness and inadequate financial infrastructure. Along with this, gender differences also exist in financial decision-making. Kale and Panchapagesan (2012) reported that poor financial literacy, weak regulatory mechanisms, and equity preference as the major challenges in the growth of the mutual fund market. In ETFs, brokerage cost, tracking error, liquidity problem and bid-ask spread are main challenges (Sayyad et al. 2025). Absence of tax benefits is also a challenge, as some countries like the USA offer significant tax benefits on ETFs as compared to active mutual funds, but in India, there is no tax advantage on ETFs.

Conclusions and Policy Implications

Mutual funds and ETFs are two important investment avenues in the Indian stock exchange market. This study attempts to provide a comparative analysis of these two investment options. The analysis reveals that both mutual funds and ETFs provide portfolio diversification under the guidance of experienced fund managers. Various types of these funds satisfy the different investment requirements of Indian retail and institutional investors. These are better investment avenues with high returns over the traditional investments in fixed income bearing assets. As the Indian economy is growing rapidly, Investors can take advantage of economic development by investing in the stock exchange through these funds. However, the funds differ in certain aspects related to management, composition, risk, return and cost structures, offering the investors a choice to invest as per their personal investment objectives.

The study also highlights different challenges faced by the Indian investment market. Major hurdles in the growth of investment in mutual funds and ETFs are poverty, limited financial and digital literacy, inadequate financial infrastructure, rural population and absence of tax benefits. Financial institutions and regulatory authorities should frame suitable policies to address these hurdles and make these investment products popular among the investors. Financial and digital literacy should be widespread with a special focus on female financial participation. Investment is the backbone of developing economies like India. The professionally managed funds like mutual funds and ETFs are most suitable in the present Indian scenario. People must be made aware of these investment options, costs should be reduced and regulatory mechanism must be strengthened to safeguard the interests of investors and build their confidence.

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