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INNOVATIVE APPROACHES TO ESTIMATE AND ANALYSE TRACKING ERRORS OF EXCHANGE TRADED FUNDS IN INDIAN STOCK MARKETS

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ABSTRACT

ETFs (Exchange Traded Funds) are the investment option that has earned popularity in last two decades. One of the primary issues that these new hybrid instruments face is their efficiency in following and adjusting to the price movements and successive returns of their benchmark assets. The deviations of these ETFs from the benchmark asset are referred to as tracking errors and the   current article attempts to explore various approaches to identify and to estimate the tracking errors of ETFs traded in NSE. For this purpose three major ETFs were selected on the basis of their average turnover and Nifty Fifty Index was chosen as the benchmark asset. Daily closing values of all the selected variable were taken for a reference period of two years ranging from 17-12-2015 to 15-12-2017.For the purpose of estimating the tracking errors, Test of Absolute Differences, Regression Estimation of Residuals along with their diagnostics and Two Sample Standard Deviation Test were applied along with t-tests and f-test The study identified the significant presence of tracking errors of these ETFs and the analysis of the results led to the conclusion that the Nifty ETFs are not efficient in following their benchmark assets and clearly indicates that the ETF's are not rigorously following the Benchmark but are deviating.

Keywords: ETFs, Tracking error, NIFTY FIFTY Index, Benchmark, Test of Absolute Differences, Regression Estimation of Residuals, Two Sample Standard Deviation Test.