An investor education initiative

Edelweiss MUTUAL FUND

Index funds: Your gateway to equity markets

There was a time when the term 'index' simply meant a list of things in alphabetical order. But if you are someone who is serious about financial planning, then the word index or more accurately the term 'index funds' can have a far more powerful meaning for you. Today, if someone asks you how the stock market is performing you will look at the returns generated by the benchmark index for example the Sensex or the Nifty. Similarly, many investors also compare the returns generated by their investment portfolio with benchmark returns to evaluate how their portfolio has fared. Since the benchmark index is pretty much the hero of the market, around whom the entire investing story revolves, wouldn't it be better to simply invest in the index?

Enter, index mutual funds, a simple and even cost effective way of investing in the index. If you are wondering what is index mutual fund and how it can add value to your portfolio then you have come to the right place. Index funds are mutual fund schemes that mimic an underlying benchmark index. This means that the index mutual fund will hold all the securities that are present in the underlying index and that too in the same proportion. For instance, if you invest in Nifty 50 index funds, your portfolio will track the movement of the Nifty 50 index, bringing you returns in line with the growth of the companies comprising the Nifty 50. You need not choose the stocks yourself, the fund will do it for you.

The working of an index fund

You must have heard of variants such as large cap index funds, liquid funds, short term funds, equity funds, etc. You must also know that your corpus should be divided among diverse investment instruments to earn optimal returns and minimise risks. Let's see how key features of index mutual funds can help you meet multiple requirements.

Diversification: Following benchmark indices like the Nifty, the Sensex or even sectoral or market capitalisation based indices, the money invested in the index fund is used to buy shares of all companies that make up the underlying index. This can help you diversify across sectors and companies through single investment. Further, the returns you earn are tied to a variety of stocks, making your portfolio that much more diversified.

Growth: While indices and markets fluctuate over the short term, history shows that they end up making strong returns over the longer term. Index mutual funds allow you to diversify your corpus across the companies which are a part of the underlying index, offering you a chance to partake in the growth of the index.

Low cost: Index mutual funds are passively managed. This means that the fund manager simply buys the same securities as the underlying index and then holds on to them unless there is a rebalancing in the index. Since the main aim is to generate market-like and not market-beating returns, the fund management expenses are relatively lower compared to actively managed funds.

Additionally, since the level of trading activity is low, index funds usually have lower transaction costs.

Investing in an index fund

You can choose to invest in an equity index fund or even a debt index fund either through a systematic investment plan (SIP) or put in lumpsum money. If you choose to invest via a SIP, then you will have the added advantage of compounding, rupee-cost averaging, and higher investment discipline. Overall, this can help you have a smooth financial planning journey and achieve your financial goals.

If you have been watching from the side lines, waiting for the push to start investing in equities, index funds are the best option for you. Now, instead of wondering what is index mutual fund, you can start investing in them by choosing the index you prefer. Truly, investing in equities was never this simple – and, you can start with as little as 500 rupee SIP!

An investor education initiative by Edelweiss Mutual Fund

All Mutual Fund Investors have to go through a onetime KYC process. Investor should deal only with Registered Mutual Fund (RMF).

For more info on KYC, RMF and procedure to lodge/redress any complaints, visit - https://www.edelweissmf.com/kyc-norms

Mutual Fund investments are subject to market risks, read all scheme related documents carefully.