



THE INDEX INVESTOR

The language of **Index Investing**



A note before you begin

Passive investing is supposed to be simple. Buy an index fund, stay invested, let the market do the work. That is the entire idea. But somewhere between opening a mutual fund account and understanding your first statement, the jargon gets in the way. Tracking error. TER. iNAV. Reconstitution. Smart beta. These words appear in fund documents, in news reports, in conversations. Most of the time, nobody stops to explain them. This booklet exists to fix that.

It is a plain-English dictionary of terms that any index investor in India will encounter. We have written each definition the way we would explain it to a friend: without assuming prior knowledge, without dressing it up, and without leaving out anything that matters. Every term includes a one-line example grounded in Indian rupees, Indian indices, and Indian tax rules, because that is the world you are investing in.

A few things this booklet is not. It is not a guide to picking funds. It is not a substitute for reading a scheme information document before you invest. And it is not exhaustive. The world of passive investing is expanding quickly, and new terms will always emerge. Think of this as a foundation, not a ceiling.

You do not need to read it cover to cover. Keep it nearby. When a term stops you mid-sentence in an article, a portfolio report, or a conversation with your advisor, look it up, understand it, and move on. The goal is not to turn you into a financial expert. It is to make sure that language never stands between you and a sound investment decision. That has always been what Value Research is here for.

Passive investing dictionary

A

Alpha: The extra return a fund earns over and above its benchmark. Positive alpha means the fund beat the index; negative alpha means it fell short.

AMC (Asset management company): The company that manages a mutual fund. It collects money from investors, invests it, and charges a fee for doing so. Example: SBI Mutual Fund, HDFC Mutual Fund, and Nippon India Mutual Fund are all AMCs.

Asset allocation: Deciding how to divide your money across different asset classes — equity, debt, gold, and so on. It is the single most important investment decision you will make. Example: A 60:40 equity-debt allocation means 60 per cent of your portfolio is in equity index funds and 40 per cent in debt index funds.

Asset class: A broad category of investment — equity, debt, gold, real estate, and so on. Each behaves differently in different market conditions. Example: When equity falls during a recession, debt often holds steady, which is why most portfolios hold both asset classes.

AUM (Assets under management): The total market value of all the money a fund manages at a given point in time. Example: If an index fund has 10 lakh investors each holding ₹10,000 worth of units, the fund's AUM is ₹1,000 crore.

B

Benchmark: The index against which a fund's performance is measured. For a large-cap index fund, the benchmark is typically the Nifty 50 or Sensex. Example: If the Nifty 50 returned 15 per cent and the index fund returned 14.8 per cent, the fund nearly matched its benchmark.

Beta: A measure of how much a fund or stock moves relative to the market. A beta of 1 means it moves in line with the index; above 1 means it moves more; below 1 means it moves less. Example: A low-volatility index fund might have a beta of 0.75, meaning it typically falls less than the market in a downturn.

Broad market index: An index that covers a wide cross-section of the stock market, not just one sector or theme. Example: The Nifty 500 is a broad market index covering 500 companies across large, mid, and small caps.

C

CAGR (Compound annual growth rate): The rate at which an investment grows each year, assuming all gains are reinvested. It is the most commonly used way to express long-term investment returns. Example: If ₹1 lakh invested in a Nifty 50 index fund became ₹3.2 lakh in 10 years, the CAGR was approximately 12.3 per cent.

Compounding: Earning returns not just on your original investment, but also on your accumulated returns. The longer you stay invested, the more powerful this becomes. Example: ₹10,000 invested at 12 per cent per year becomes ₹31,058 in 10 years and ₹96,463 in 20 years — the difference is compounding.

Concentration risk: The risk of putting too much money in one stock, sector, or asset class. A well-diversified index fund reduces this risk. Example: An index fund tracking only IT stocks carries concentration risk — if the sector falls, so does the entire fund.

Constituent: A stock or bond that is part of an index. Together, all constituents make up the index. Example: Reliance Industries, HDFC Bank, and Infosys are among the 50 constituents of the Nifty 50.

D

Debt index fund: An index fund that tracks a fixed-income index — investing in government bonds, corporate bonds, or treasury bills — rather than stocks. Example: A fund tracking a Nifty G-Sec index invests in central government bonds and is suitable for conservative investors.

Direct plan: A mutual fund plan where you invest directly with the fund house, without going through a distributor. Because no commission is paid to a middleman, the expense ratio is lower. Example: The direct plan of a Nifty 50 index fund might have an expense ratio of 0.1 per cent, versus 0.5 per cent for the regular plan.

Distribution (IDCW): Short for Income Distribution cum Capital Withdrawal. Previously called a dividend, this is when a fund pays out part of its earnings to investors. For index funds, the growth option is generally more tax-efficient. Example: An index fund on the IDCW option might periodically pay ₹2 per unit, which is taxed as per the investor's income tax slab.

Diversification: Spreading your money across many different investments so that a loss in one does not wipe out your entire portfolio. Example: A Nifty 50 index fund automatically diversifies your money across 50 large companies in different sectors.

Drawdown: The percentage fall from a fund's peak value to its lowest point over a given period. It measures how much you could have lost in the worst case. Example: During the Covid crash in March 2020, the Nifty 50 fell nearly 40 per cent from its January 2020 peak.

Duration: A measure of how sensitive a debt fund is to interest rate changes. The higher the duration, the more the fund's value moves when interest rates change. Example: A target maturity debt index fund with a 10-year duration will fall more in value than a short-duration fund if interest rates rise by 1 per cent.

E

Equity: Ownership in a company. When you buy a stock or invest in an equity index fund, you own a tiny piece of many businesses. Example: An equity index fund tracking the Nifty 100 gives you fractional ownership in 100 of India's largest companies.

ETF (Exchange-traded fund): A fund that trades on a stock exchange, just like a share. It typically tracks an index and can be bought or sold throughout the day at market prices. Example: The Nippon India ETF Nifty 50 BeES tracks the Nifty 50 and can be bought on the NSE just like you would buy a share of Infosys.

Expense ratio: The annual fee a fund charges investors to manage the portfolio, expressed as a percentage of AUM. In an index fund, this is typically very low. Example: An expense ratio of 0.2 per cent on a ₹1 lakh investment means you pay ₹200 a year — it is deducted automatically from the fund's NAV.

F

Factor investing: A strategy of investing in stocks that share a particular characteristic — like quality, value, or momentum — based on research showing these factors have historically delivered better risk-adjusted returns. Example: A quality factor index fund picks companies with high returns on equity and low debt, based on the belief that such businesses compound wealth steadily over time.

Flexi-cap index fund: An index fund that tracks an index covering stocks across market capitalisations — large, mid, and small cap — in a flexible ratio. Example: A fund tracking the Nifty 500 index gives exposure to companies of all sizes in a single fund.

Free-float market capitalisation: The market value of only those shares that are freely available for trading — excluding shares held by promoters, governments, and strategic investors. Example: Even though a company's total market cap is ₹2 lakh crore, its free-float market cap might be lower because the promoter holds 60 per cent of the shares.

Fund house: Another term for an AMC. The organisation that creates and manages mutual funds. Example: ICICI Prudential Mutual Fund and Mirae Asset Mutual Fund are fund houses that offer index funds.

Fund of funds (FoF): A mutual fund that invests in other mutual funds rather than directly in stocks or bonds. International index FoFs invest in overseas funds. Example: A fund of funds investing in an S&P 500 ETF allows Indian investors to get exposure to US stocks without a foreign brokerage account.

G

G-Sec (Government securities): Bonds issued by the central government to borrow money. They are considered the safest fixed-income instruments in India. Example: A debt index fund tracking the Nifty G-Sec index invests only in central government bonds.

Gold ETF: An ETF that tracks the domestic price of gold, allowing investors to hold gold in electronic form without physical storage. Unit sizes vary by fund house — always check the scheme information document for the exact gold equivalent per unit. Example: Buying units of a gold ETF gives you exposure to gold at the prevailing domestic price, without worrying about storage, purity, or making charges.

H

Holding period: The length of time you hold an investment before selling. This matters because tax treatment depends on how long you have held the investment. Example: Selling equity index fund units within 12 months means paying 20 per cent short-term capital gains tax; holding beyond 12 months means paying 12.5 per cent long-term capital gains tax on gains above ₹1.25 lakh. For debt index funds purchased on or after April 1, 2023, all gains are taxed at your income slab rate, regardless of how long you hold.

I

Index: A list of stocks (or bonds) selected by an index provider based on specific rules. It represents a particular part of the market — a country, a sector, a market cap range, or a factor. Example: The Nifty 50 is an index of 50 of the largest and most liquid stocks on the NSE, representing over 60 per cent of the free-float market capitalisation of all stocks listed on the NSE.

Index fund: A mutual fund that invests in the exact same stocks as a specific index, in the same proportions, with the goal of matching — not beating — the index's returns. Example: A Nifty 50 index fund buys shares of all 50 Nifty companies in proportion to their weight, so its returns mirror the index.

Index provider: The organisation responsible for creating, maintaining, and updating an index. They decide which stocks are included, how they are weighted, and when the index is reconstituted. Example: NSE Indices is the index provider for the Nifty family of indices.

Index replication: The method a fund uses to match its benchmark index. Full replication means buying every stock in the index; partial replication means buying a representative subset. Example: A Nifty 50 index fund uses full replication — it buys all 50 stocks in the index.

iNAV (Indicative NAV): The real-time estimated value of an ETF's underlying portfolio, calculated and published throughout the trading day. It helps you judge whether the ETF is trading at a fair price on the exchange. Example: If the iNAV of a Nifty ETF is ₹200 but it is trading at ₹202 on the exchange, the ETF is trading at a premium.

L

Large-cap: As defined by SEBI, companies ranked 1 to 100 by market capitalisation on Indian exchanges. Large-cap index funds are the most commonly recommended starting point for passive investors. Example: An index fund tracking the Nifty 100 invests in the 100 largest companies by market cap, including names like Reliance, TCS, and HDFC Bank.

Liquid ETF: An ETF that invests in very short-term government securities and is used to park cash temporarily. It earns a small return while keeping your money easily accessible. Example: Traders sometimes park idle cash in a liquid ETF overnight rather than leaving it in a zero-interest trading account.

Liquidity: How easily you can buy or sell an investment without significantly affecting its price. High liquidity means you can transact quickly at fair prices. Example: A large Nifty ETF with ₹20,000 crore in AUM is highly liquid — you can buy or sell thousands of units without moving the price.

LTCG (Long-term capital gains): Profits from selling an investment held for longer than the minimum qualifying period. For equity funds, the threshold is 12 months; for debt funds purchased on or after April 1, 2023, there is no LTCG benefit — all gains are taxed at the slab rate. For older debt fund purchases (before April 1, 2023), the LTCG threshold is 24 months. Example: If you sell equity index fund units after 18 months and make a profit, the gains above ₹1.25 lakh are taxed at 12.5 per cent as LTCG.

M

Market capitalisation (Market cap): The total market value of a company — calculated by multiplying its share price by the total number of shares outstanding. Example: If a company has 100 crore shares outstanding and the share price is ₹500, its market cap is ₹50,000 crore.

Maximum drawdown: The largest peak-to-trough decline in a fund's value over a given period. It shows the worst-case loss an investor would have experienced. Example: The Nifty 50's maximum drawdown during the 2008 financial crisis was about 60 per cent from peak to trough.

Mid-cap: As defined by SEBI, companies ranked 101 to 250 by market capitalisation on Indian exchanges. They offer higher growth potential than large caps, but with more volatility. Example: A Nifty Midcap 150 index fund gives you diversified exposure to mid-sized businesses across sectors.

N

NAV (Net asset value): The per-unit value of a mutual fund, calculated by dividing the total value of all its holdings by the number of units outstanding. Published once daily, after market close. Example: If a Nifty 50 index fund holds stocks worth ₹1,000 crore and has 10 crore units outstanding, the NAV is ₹100 per unit.

NFO (New fund offer): The period when a new mutual fund is launched and units are offered to investors for the first time, typically at ₹10 per unit. Example: When a fund house launches a new Nifty Midcap 150 index fund, it opens an NFO for 15 days during which investors can subscribe.

Nifty 50: India's most widely followed stock market index, comprising 50 large and liquid companies listed on the National Stock Exchange (NSE). It represents over 60 per cent of the free-float market capitalisation of all stocks listed on the NSE. Example: When you hear "the market rose 1.5 per cent today," it usually refers to the Nifty 50.

Nifty Next 50: An index of the 51st to 100th largest companies on the NSE by market cap. It is often considered a blend of large-cap stability and mid-cap growth potential. Example: Companies that grow large enough may eventually graduate from the Nifty Next 50 into the Nifty 50.

Nifty 100: The combination of the Nifty 50 and the Nifty Next 50 — India's 100 largest companies by free-float market cap. Example: A Nifty 100 index fund offers slightly more diversification than a Nifty 50 fund by including the next 50 large companies.

O

Overlap: When two index funds you hold contain many of the same stocks, it reduces the diversification benefit of owning both. Example: A Nifty 50 fund and a Nifty 100 fund have 50 per cent overlap — half the stocks are the same — so holding both may not diversify you as much as you think.

P

Passive investing: An investment approach that aims to match the returns of a market index, rather than beat it. It involves low costs, minimal trading, and no stock selection. Example: Instead of paying a fund manager to pick stocks, a passive investor simply buys a Nifty 50 index fund and holds it for years.

Premium / Discount (ETF): When an ETF trades above (premium) or below (discount) its net asset value on the exchange. Example: If an ETF's NAV is ₹100 but it is trading at ₹101 on the exchange, it is trading at a 1 per cent premium.

R

Rebalancing: Adjusting your portfolio periodically to bring it back to your target asset allocation — selling what has grown too large and buying what has shrunk. Example: If your target was 70:30 equity-debt but a bull market pushed equity to 80 per cent, you sell some equity index fund units and buy more debt index fund units to rebalance.

Reconstitution: The process by which an index adds, removes, or re-weights its constituent stocks. Most major Indian indices reconstitute twice a year. Example: When a company in the Nifty Next 50 grows large enough to qualify, it may be promoted to the Nifty 50 at the next reconstitution — and a fund tracking the Nifty 50 automatically buys it.

Regular plan: A mutual fund plan where a distributor or advisor is involved in the transaction. A portion of the expense ratio is paid to them as commission, making regular plans more expensive than direct plans. Example: The regular plan of a Nifty 50 index fund might have an expense ratio of 0.5 per cent versus 0.1 per cent for the direct plan — the 0.4 per cent difference compounds significantly over 20 years.

Rolling returns: A way of measuring a fund's return by calculating performance over overlapping periods — such as every one-year period over the last 10 years — rather than a single start-to-end return. Example: Instead of checking how the Nifty 50 performed from 2015 to 2025, rolling returns check how it performed in every 5-year window since 2000, giving a more honest picture of consistency.

S

Sectoral index: An index covering only one industry or sector, such as banking, technology, pharma, or infrastructure. Example: The Nifty Bank index tracks only banking stocks — a sectoral index fund tracking it rises and falls with the fortunes of the banking industry alone.

Sensex (BSE 30): India's oldest stock market index, comprising 30 large companies listed on the Bombay Stock Exchange (BSE). It is often used interchangeably with the Nifty 50 in news reports. Example: When the Sensex crossed 80,000 for the first time, it was a widely reported milestone for the Indian market.

SIP (Systematic investment plan): A method of investing a fixed amount at regular intervals — monthly or quarterly — into a mutual fund, regardless of market conditions. It is the most recommended way to invest in index funds. Example: An SIP of ₹5,000 a month in a Nifty 50 index fund, held for 20 years at a 12 per cent annual return, would grow to approximately ₹50 lakh.

Small-cap: As defined by SEBI, companies ranked 251 and beyond by market capitalisation on Indian exchanges. They offer the highest potential growth but also the highest volatility. Example: A Nifty Smallcap 250 index fund invests across hundreds of smaller businesses — more risk, but also the chance of higher long-term returns.

T

Target maturity fund: A debt index fund with a fixed end date. It invests in government or corporate bonds that mature around the same time as the fund, giving investors visibility on expected returns if they hold until maturity. Example: A target maturity fund maturing in April 2030 invests in bonds maturing by 2030 — if you hold until then, your return is roughly predictable from the day you invest.

TER (Total expense ratio): The same as the expense ratio — the all-in annual cost of running the fund, expressed as a percentage of AUM. It is already deducted from the NAV daily, so you never receive a separate bill. Example: A Nifty 50 index fund with a TER of 0.1 per cent charges ₹100 a year on a ₹1 lakh investment.

Thematic index: An index built around a broad theme — such as consumption, digital economy, ESG (environmental, social, governance), or manufacturing — rather than a single sector. Example: An ESG index fund tracks companies that score well on environmental and governance criteria, filtering out businesses with poor practices.

Total returns index (TRI): An index that includes both price appreciation and dividends reinvested. It is the correct benchmark to use when comparing a fund's performance, because equity funds themselves reinvest dividends. Example: If the Nifty 50 TRI returned 13 per cent but the price return showed 12 per cent, the roughly 1 per cent difference represents dividends paid by the index companies.

Tracking difference: The gap between a fund's actual return and its benchmark index's return over a given period. Unlike tracking error, which measures consistency, tracking difference measures the total shortfall. Example: If the Nifty 50 TRI returned 15 per cent in a year and the index fund returned 14.8 per cent, the tracking difference is 0.2 per cent.

Tracking error: A measure of how consistently a fund follows its benchmark, expressed as the standard deviation of daily or weekly return differences. Lower is better for a passive fund. Example: A Nifty 50 index fund with a tracking error of 0.05 per cent is closely hugging its benchmark; one with 0.5 per cent is wandering.

U

Unit: A single share of a mutual fund or ETF. When you invest in a fund, you receive units proportional to the amount you invest. Example: If the NAV of an index fund is ₹50 and you invest ₹5,000, you receive 100 units.

V

Volatility: The degree to which an investment's price fluctuates over time. High volatility means big swings up and down; low volatility means steadier returns. Example: Small-cap index funds have high volatility — they might return 60 per cent one year and fall 40 per cent the next.

W

Weightage (Weight): The proportion of a single stock in an index, expressed as a percentage. In a market-cap-weighted index, larger companies have higher weights. Example: If Reliance Industries makes up about 9 per cent of the Nifty 50, it has a weight of 9 per cent — meaning 9 per cent of your fund's money is in Reliance.

X

XIRR (Extended internal rate of return): A method of calculating returns when money is invested or withdrawn at irregular intervals — for example, through an SIP. More accurate than simple CAGR for real-world portfolios. Example: If you invested ₹5,000 a month via SIP and want to know your true annualised return, XIRR gives you the correct answer — your mutual fund app calculates this automatically.

Y

Yield: The income generated by a fixed-income investment, expressed as a percentage of its price. For debt index funds, it indicates how much the underlying bonds are earning. Example: If a debt index fund holds bonds with an average yield of 7.2 per cent per annum, that is roughly what you can expect to earn if you hold until maturity.

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