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Malaysian Exchange-Traded Fund versus Unit Trust: Which One is Better?

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Abstract

Exchange-traded funds (ETFs) offer a convenient and cost-effective way for investors to invest in various securities. Frequently, ETFs are mistakenly identified as unit trusts. Although they share some similar characteristics, they are actually different. This study uses three and five years of data to examine the performance of a Malaysian ETF and three unit trust funds. The performances of these funds are evaluated using the Sharpe and Treynor ratios, with FTSE Bursa Malaysia KLCI being used as the benchmark. Results reveal that unit trusts generally outperform during the periods under study. Nevertheless, despite this performance difference, ETFs' lower expenses, flexibility, transparency, and strategic benefits present strong arguments against their complete dismissal. Therefore, integrating ETFs into an investment portfolio can contribute to long-term growth and stability, underscoring their value despite comparative performance with unit trusts. The findings of this study may be applied to help investors and fund managers make informed decisions to improve portfolio performance.

Keywords
Equity, Exchange Traded Funds, Unit Trusts, Treynor Ratio, Sharpe Ratio

1.0 Introduction

Making an investment decision is frequently more challenging than depositing money into a savings account. In today's financial landscape, the investment market has grown increasingly intricate, offering a diverse range of investment products to cater for the unique needs of investors. Each investor has different risk tolerance, personal preferences, and circumstances, which shape their investment objectives and time horizons. Some sophisticated products require more skills and knowledge for investors to make informed decisions. That is why some may entrust professional managers with their investments, especially if they are new to investing, have limited capital, or possess limited knowledge and expertise. Two investment products that fall under this category are exchange-traded funds (ETFs) and unit trust funds. These two investment products are often recommended for beginners. Although ETFs are frequently mistaken for unit trusts, they are not the same. While they may share some similarities, they are two different investment products. This begs the question: "Which of these two options is superior?" This study aims to answer this question.

Broadly speaking, an ETF is a passively managed fund that mirrors the performance of an index. Investors in ETF units benefit from diversification, as the fund comprises multiple securities mirroring its benchmark index. However, not all ETFs are passively managed ETFs. There are also actively managed ETFs as the market advances to fulfil various investors' demands. Unlike passively managed ETFs, which attempt to track their benchmarks, actively managed ETFs intend to outperform them. Nevertheless, passively managed ETFs are more well-known to many, especially retail investors. In Malaysia, the Securities Commission's (SC) guidelines on ETFs do not permit active ETFs to be listed on Bursa. As an ETF does

not aim to outperform the market, it can be seen as its principal drawback. Its structure is designed to match the index's performance rather than surpass it or achieve the best possible results. For instance, an increase in the benchmark index's price corresponds to a rise in the associated ETF, and vice versa. Furthermore, an ETF typically does not take temporary defensive measures due to its passive management style, even during adverse market conditions.

Exchange traded fund is a hybrid investment product with the characteristics of a unit trust and a stock. Although it may behave like an open-ended fund, it is traded like a common stock on a stock exchange. Thus, its prices fluctuate based on supply and demand. It offers high liquidity investment because it is traded on the exchange and has at least one market maker. The market maker can further enhance the market liquidity by providing a competitive bid/ask price. Initially developed to match the performance of the tracked index, it is a type of passive investment that requires little knowledge of investing. Offered by professional fund managers and well-diversified, the overall risk, especially firm-specific or unsystematic risk, is usually low. An investor only needs to do one transaction to gain exposure to the different securities in the index. Returns from ETF are earned by capital appreciation and based on the fund's underlying securities, such as dividends for stocks or interest for fixed-income securities.

Unit trusts, popularly known as mutual funds in some places, are a type of collective investment where investors can combine their funds to invest in a portfolio of assets. In other words, it pools money from many investors to invest in a wide range of assets or securities to develop a diversified portfolio. Investors do not directly purchase the securities in the portfolio; instead, the fund's ownership is divided into units of entitlement. The value of each unit is directly proportional to the fund's value. It is an easily accessible, affordable, professionally managed fund suitable for everyone, especially those who have started investing. The return on investment in unit trust is the form of income distribution and capital appreciation.

Many types of unit trusts are available for investors to choose to suit their risk appetite. For example, there are equity, fixed-income, balanced, and money market funds. Each unit trust fund has its own investment objective and strategy, so investors, especially beginners, should choose appropriate funds for their portfolio (Khairuddin et al. 2021). The equity unit trust, which primarily invests in equities or securities of listed companies, is one of the most popular types of unit trust. A diverse range of equity unit trusts, with varying risk and return rates, are on the market. An example would be an equity unit trust fund that invests in the companies listed on Bursa Malaysia. Hence, Bursa Malaysia's performance will influence the fund's performance, where a rising market will generally give rise to an increase in the unit's value and vice-versa.

Unlike ETFs, unit trust funds are designed to outperform their benchmark index. This feature can be particularly appealing to potential investors. This focus on outperformance often puts unit trust funds in the spotlight. However, the performance of the funds may vary significantly based on the types of funds. A study by Abdullah and Shari (2019) showed that the performance of equity and fixed-income funds differs significantly, as does the performance between growth and value funds compared to fixed-income funds. While it is true that an exceptional unit trust fund may surpass the market, it is important to note that this potential for higher returns also comes with higher associated risks.

On the one hand, like ETFs, a unit trust fund offers investors the opportunity to invest in a diversified portfolio. On the other hand, ETFs have an advantage over unit trusts due to their lower cost structure. The

management fee of an ETF is generally cheaper than a unit trust fund's fee, leading to a smaller percentage of the investment going toward management fees. ETFs usually have lower management fees, typically below 1% (FAQs on Exchange Traded Funds (ETFs), n.d.).

In contrast, actively managed unit trust funds usually require higher management fees due to their active investment style. Additionally, no sales charge is imposed on ETF transactions like those incurred when investing in a unit trust fund. Typically, the upfront sales fee of unit trust transactions is between 3% and 5% of the total value. The reason is that ETFs are traded on an exchange, whereas unit trusts are not. The ETF transactions are carried out through a broker, while an agent carries out the unit trust transactions. However, it is essential to note that broker fees and fees related to securities trading may still apply. Investors must consider the fees to make wise investment decisions because they will impact the returns received. In general, ETFs are perceived to be more cost-effective than unit trust funds because of their lower cost structure (Armour, 2024).

This study's main objective is to examine Malaysian ETFs' performance compared to the unit trusts' performance. In other words, this study examines the performance of Malaysian exchange-traded funds and unit trusts. Are there any differences between these two investment products? Should an investor be concerned about choosing between these two? Which one gives higher returns? This study attempts to examine the performance of Malaysian ETFs and equity unit trust funds using the Sharpe and Treynor measures. To the best of the authors' knowledge, no study has been conducted comparing Malaysian ETFs and unit trusts. This study aims to fill the gap, and it is hypothesized that these funds will provide different outcomes in terms of risk and return.

2.0 Literature Review

Modern Portfolio Theory (MPT) uses diversification to lower the risk by investing in multiple assets (Markowitz, 1952). It is a strategy for selecting securities to maximize returns while managing risk. In other words, an approach of selecting securities to form a portfolio to maximize the returns for a given level of risk. It is not simply just a theoretical concept but a practical approach. Investors can construct an optimal portfolio by diversifying across various asset classes to minimize risk while maximizing returns, reflecting the main element of this theory: diversification. Investors will always choose the less risky portfolio for a given expected return. For that reason, the concept of efficient frontier is introduced to help investors form an optimal portfolio.

Efficient frontiers consist of investment combinations with the best risk-return tradeoff. Simply put, MPT underscores the importance of asset correlation for optimal portfolio results. A well-diversified portfolio can provide lower risk for a given return level than individual assets. This theory forms the basis for many investment strategies. In line with MPT’s principles, this theory can be applied to optimize investment strategies and create a diversified portfolio when considering ETFs and unit trusts. Both investment funds offer investors a convenient way to diversify by offering diversified exposure to a wide range of assets. Applying Modern Portfolio Theory to investing in these two funds underscores the importance of diversification and the efficient allocation of assets. This theory provides a solid framework for designing investment strategies that suit individual financial goals and risk tolerance. By carefully considering the

principles of MPT and the specific characteristics of ETFs and unit trust, investors can build well-positioned portfolios for long-term investment.

There are quite a few studies that examine the performance of ETFs worldwide. For example, Stefanus and Robiyanto (2020) examined the performance of twelve exchange-traded funds in Indonesia. They used Treynor ratio, Sharpe ratio, Sortino ratio, Jensen Alpha, information ratio, and Omega ratio to measure performance. They found that only two exchange-traded funds perform better than risk-free investments using Sharpe ratio, Sortino ratio, information ratio, and Omega ratio. Meanwhile, the Treynor ratio and Jensen Alpha values were either negative or worse than risk-free investments.

In relation to that, Alamelu and Goyal (2022) examined how well 27 Indian equity ETFs traded on the National Stock Exchange of India from 2015 to 2019 replicated the performance of their benchmark indices. They found that most ETFs in the sample outperformed their underlying indices during the study period. However, significant tracking errors were observed. Additionally, the study revealed that returns from the ETFs in the sample showed a strong positive correlation with index returns while demonstrating an inverse relationship with risk levels and management fees.

Prior to that, a significant study by Kunjal et al. (2021) investigated the performance of South African ETFs in varying market conditions. The results indicated that, on average, ETFs were more responsive to changes in the underlying index during bullish markets but exhibited more significant tracking errors during bearish periods. These findings underscore the importance of understanding ETF performance in different market conditions, as it can help investors assess their risk exposure when making investment decisions. Due to the popularity and growth of ETFs as investment alternatives, Sharifzadeh and Hojat (2012investigated whether the high demand for ETFs can be explained through their outperformance compared with other passive index mutual funds. However, the study's results indicate no statistically significant difference in performance between these two types of funds. The results also revealed that product characteristics and tax benefits influence investors' selection.

Other studies assessed ETF performance based on tracking errors. The studies' findings revealed that ETFs did not track their benchmarks perfectly (see for example, Shin and Soydemir, 2010; Chu, 2013; Chen et al., 2017; Dorocáková, 2017). Shin and Soydemir (2010) asserted that the tracking errors of 26 ETFs from Asia, Europe and the United States are persistent and significantly different from zero. The deviation was more extensive for Asian ETFs comprising more emerging markets. Likewise, Chu (2013) revealed that tracking errors of Hong Kong ETFs were comparatively more significant than those of American and Australian ETFs. The findings indicated that the funds cannot easily replicate the performance of the underlying indices, thus implying that ETF investors may face additional risks as a result of investing in ETFs.

Similarly, Chen et al. (2017) found that New Zealand ETFs had substantial price deviation from their underlying indices based on daily and monthly data. Their findings indicated that New Zealand ETFs did not track their underlying index perfectly. They also showed that these ETFs' tracking errors were more significant than those observed in other countries. The implication of this finding indicated that investors should be aware that the exposure of investing in ETFs may not be the same as the underlying index. In other words, it cannot be assumed that the risk is the same just because ETFs are commonly known as

passively managed funds. ETFs should be more concerned regarding the risk and return, especially if the tracking error is substantially large. A study by Dorocáková (2017) further revealed that the deviation of ETFs' performance from their benchmarks was seasonal, particularly towards the end of the year. It was also shown that fund size and fund's stock consolidation are the factors that influence the deviation (Dorocáková, 2017).

Tsalikis and Papadopoulos (2019) compared tracking errors in American and European ETFs. They argued that American ETFs experienced lower tracking errors than European ETFs. They used three tracking error measurements: the standard deviation of the return differences between the ETF and its benchmark index, the absolute difference in returns between the ETF and the index and the standard errors from the regression analysis based on daily data. In brief, past studies provided inconclusive findings of ETFs' returns, and many past studies indicated a deviation in ETFs' performance compared to their benchmarks.

3.0 Methods

The main objective of this study is to compare the performance of Malaysian ETFs with the performance of Malaysian unit trusts. To achieve this objective, Sharpe and Treynor ratios are used to measure the funds' performance. The funds employed in this study are FTSE Bursa Malaysia KLCI ETF, Affin Hwang Equity, Principal KLCI-Linked Fund and AmMalaysia Equity. FBMKLCI serves as the benchmark for proxying market returns, and the Malaysian 3-month Treasury Bills serve as a proxy for the risk-free rate of return. This study utilizes monthly returns of unit trust funds, FBMKLCI ETF, 3-month Malaysian Treasury Bills, and FBMKLCI. The study spans from January 2018 to December 2022. The data starts from 2018 to incorporate the 3-year and 5-year periods. Practically, 3-year or 5-year periods reflect appropriate periods for trends and performance analyses by smoothing out temporary volatility. Shorter periods, like one year, can easily be influenced by market fluctuations or external events.

The FTSE Bursa Malaysia KLCI ETF (FBMKLCI-EA) became the inaugural equity ETF in Malaysia when it was listed on July 19, 2007. Its underlying index is the FTSE Bursa Malaysia KLCI Index. This index comprises the 30 largest companies listed on Bursa Malaysia based on market capitalization. It was initially known as the FBM30 ETF but then changed to FBM KLCI ETF when the FBM KLCI was launched on July 6 2009. FTSE Bursa Malaysia KLCI ETF allows investors to own the top 30 Malaysian companies by making only one transaction. It is designed to replicate the performance of FTSE Bursa Malaysia KLCI. Specifically, its objective is "to achieve a price and yield performance, before fees, expenses, and tax, that is generally similar to that of the Benchmark, balanced with the need to facilitate liquidity provision" (www.fbmklcietf.com.my, n.d.). The trading board has a lot size requirement of 100 units and applies a management fee of 0.50% per year based on the fund's NAV. The fee is relatively small compared to the typical fee for actively managed unit trusts, usually between 1.5% and 2%. In addition, subject to a minimum of RM40, there is usually a brokerage fee of 0.70% of the contract value.

Affin Hwang Equity Fund prioritizes investments in equities and equity-linked instruments, allocating between 70% to 99.8% of its portfolio towards these assets, with a maximum of 30% allowed for fixed-income instruments. The fund imposes a management fee of up to 1.50% per annum based on the Net Asset Value (NAV). Principal KLCI-Linked Fund focuses on securities and permissible investments, with up to 99.5% invested in these assets and at least 0.5% in liquid assets. It carries a management fee of up to 0.95% per annum of the NAV. AmMalaysia Equity Fund targets between 75% to 98% of its NAV in equities, with

2% to 25% allocated to cash and liquid assets. Like Affin Hwang, it also applies a management fee of up to 1.50% per annum of the NAV.

Treynor and Sharpe ratios are widely used to measure a fund's performance. They provide investors and analysts with insights into how effectively a portfolio generates returns while considering the level of risk taken. The Sharpe ratio, introduced by William F. Sharpe in 1966, focuses on the risk-adjusted return using total risk (systematic and unsystematic risks), represented by standard deviation. This ratio measures how well a portfolio's returns compensate for the overall risk taken (Sharpe, 1966). A higher Sharpe ratio implies better risk-adjusted returns. The formula for the Sharpe ratio is as follows:
Sharpe Ratio = (Portfolio Return – Risk Free Rate) ÷ Standard Deviation of Portfolio Returns

Jack Treynor developed the Treynor ratio to determine how much excess return is generated for each unit of risk a portfolio takes. In other words, the ratio measures the risk-adjusted return of a fund or a portfolio. This ratio assesses the portfolio's excess return (return above the risk-free rate) per unit of systematic risk, proxied by beta. A higher Treynor ratio indicates that the portfolio generates a better return than its systematic risk. Treynor ratio offers information on how efficiently a portfolio uses its systematic risk to generate returns (Treynor, 2012). The formula for the Treynor ratio is as follows:
Treynor Ratio= (Portfolio Return – Risk Free Rate) ÷ Beta of Portfolio Returns

In essence, while both ratios evaluate risk-adjusted returns, they vary in the type of risk they take into consideration. The Treynor ratio assesses performance relative to systematic risk (beta). In contrast, the Sharpe ratio considers total risk (standard deviation). Investors who perceive their portfolios as well-diversified might favor the Treynor ratio for its exclusive focus on systematic risk. Conversely, those prioritizing comprehensive portfolio risk assessment may lean towards the Sharpe ratio.

4.0 Results and Discussion

Table 1 presents a summary of returns, risks, and performance measures of the FBMKLCI ETF, the benchmark index, and the three selected equity funds from 2020 to 2022.

Table 1: Performance of Selected Funds for 3-Year Period (2020 – 2022)

Funds	Mean (%)	SD (%)	Sharpe	Beta	Treynor
FBMKLCI ETF	-0.1507	4.1580	0.0181	0.9731	0.0008
FBMKLCI	-0.1681	4.2136	0.0138	1.0000	0.0006
Affin Hwang Equity	0.4427	5.0942	0.1313	0.9090	0.0074
AmMalaysia Equity	0.5073	5.5197	0.1329	0.9787	0.0075
Principal KLCI-Linked Fund	0.0429	4.0605	0.0662	0.9594	0.0028

Based on data shown in Table 1, AmMalaysia Equity has the highest average return (0.5073%), followed by Affin Hwang Equity (0.4427%). On average, FBMKLCI ETF and FBMKLCI experience a loss over the three years, -0.1507% and -0.1681%. At the same time, the Principal KLCI-Linked Fund has a slightly positive mean return (0.0429%). AmMalaysia Equity has the highest standard deviation (5.5197%), indicating higher volatility in line with the notation of high-risk, high-return. Principal KLCI-Linked Fund has the lowest standard deviation (4.0605%), indicating lower volatility. FBMKLCI ETF and FBMKLCI

have similar volatility mainly due to how an ETF is structured. In the same vein, the betas of all funds are nearing the market's beta, indicating their volatilities are less than the market's. Specifically, all funds demonstrate a beta of around 0.9, highlighting their lower volatility compared to the market.

The results of the Sharpe measures reveal that AmMalaysia Equity has the highest Sharpe ratio (0.1329), signifying the best risk-adjusted return. In second place is Affin Hwang Equity (0.1313), and in third place is Principal KLCI-Linked Fund (0.0662). The ETF, with a Sharpe ratio of 0.0181, secures fourth place ahead of FBMKLCI. The close ranks between the ETF and FBMKLCI are expected, given that the ETF is designed to track the performance of its underlying index.

Likewise, the ranks of the funds based on Treynor measures are the same. AmMalaysia Equity has the highest Treynor ratio (0.0075), indicating the best return per unit of market risk. Affin Hwang Equity follows with a Treynor ratio of 0.0074. Like the positions for Sharpe measures, ETF comes fourth with 0.0008 and FBMKLCI fifth with 0.0006.

In summary, for the three-year period (2020 to 2022), AmMalaysia Equity stands out with the highest mean return, Sharpe ratio, and Treynor ratio, indicating strong performance and good risk-adjusted returns. FBMKLCI appears to have the poorest performance with negative mean return, lowest Sharpe ratio, and lowest Treynor ratio. AmMalaysia Equity and Affin Hwang Equity have higher standard deviations, indicating higher risk. In contrast, the Principal KLCI-Linked Fund has the lowest standard deviation among the unit trusts, indicating lower risk, where it also gives lower returns. The results also indicate that the performance of the ETF and FBMKLCI are similar, indicating their close associations. While unit trusts aim to beat the market, ETFs aim to track their benchmark closely.

Table 2 presents a summary of returns, risks, and performance measures of the FBMKLCI ETF, the benchmarking index, and the three selected equity funds from 2018 to 2022.

Table 2: Performance of Selected Funds for 5-Year Period (2018 – 2022)

Funds	Mean (%)	SD (%)	Sharpe	Beta	Treynor
FBMKLCI ETF	-0.2992	3.5989	-0.0335	0.9644	-0.0013
FBMKLCI	-0.3059	3.6727	-0.0347	1.0000	-0.0013
Affin Hwang Equity	0.1996	4.1968	0.0901	0.8490	0.0045
AmMalaysia Equity	0.5347	4.6229	0.1543	0.8270	0.0086
Principal KLCI-Linked Fund	-0.1027	3.5380	0.0214	0.9588	0.0008

Overall, the findings for the five years are very similar to the three-year period in ranking based on Sharpe and Treynor measures. However, unlike the three-year findings, only two unit trust funds exhibit positive average returns. AmMalaysia Equity has the highest average return (0.5347%). Affin Hwang Equity shows a positive mean return of 0.1996%, while Principal KLCI-Linked Fund shows a negative mean return of -0.1027%. In short, the ETF, FBMKLCI and Principal KLCI-Linked Fund experience an average loss over the five years.

As for standard deviation, AmMalaysia Equity has the highest (4.6229%), indicating the highest volatility compared to the others. In contrast, the Principal KLCI-Linked Fund has the lowest (3.5380%), indicating

the lowest volatility. Serving as the benchmark, FBMKLCI has a beta of 1.0000. Similar to the three-year findings, all funds have betas less than 1. However, for the five-year period, AmMalaysia Equity has the lowest beta (0.8270), indicating it is less volatile compared to the market. Affin Hwang Equity has a beta of 0.8490, while Principal KLCI-Linked Fund and ETF have betas close to 1, suggesting similar volatility to the market.

The funds' ranks are the same for five years as the three years. AmMalaysia Equity has the highest Sharpe ratio (0.1543), placing it first. Then, in second place is Affin Hwang Equity, with a Sharpe ratio of 0.0901. KLCI has the lowest Sharpe ratio (-0.0347), indicating the poorest risk-adjusted return among the funds. Third is the Principal KLCI-Linked Fund, which has a ratio of 0.0214, followed by ETF, which has a ratio of -0.0335. In brief, the fund's rank for the five years does not change compared to the three years, revealing superior performance by AmMalaysia Equity, while FBMKLCI is not very good. Similar results are observed for the Treynor measures. A slight difference between the Treynor measure for five years and three years is that the ETF and FBMKLCI show the same ratio, placing both in last place and indicating the lowest return per unit of market risk.

In brief, the AmMalaysia Equity fund stands out with the highest mean return, Sharpe ratio, and Treynor ratio, indicating strong performance and good risk-adjusted returns. In contrast, FBMKLCI appears to have the poorest performance, with the lowest Sharpe ratio and Treynor ratio.

Comparison between Three Years and Five Years Performance

This section provides a detailed comparison of the fund's performance over three and five years to identify trends in average returns, standard deviation, beta, Sharpe ratio, and Treynor ratio.

Table 3: Average Returns of Three Years versus Five Years

Funds	Mean (%) – 3 years	Mean (%) – 5 years
FBMKLCI ETF	-0.1507	-0.2992
FBMKLCI	-0.1681	-0.3059
Affin Hwang Equity	0.4427	0.1996
AmMalaysia Equity	0.5073	0.5347
Principal KLCI-Linked Fund	0.0429	-0.1027

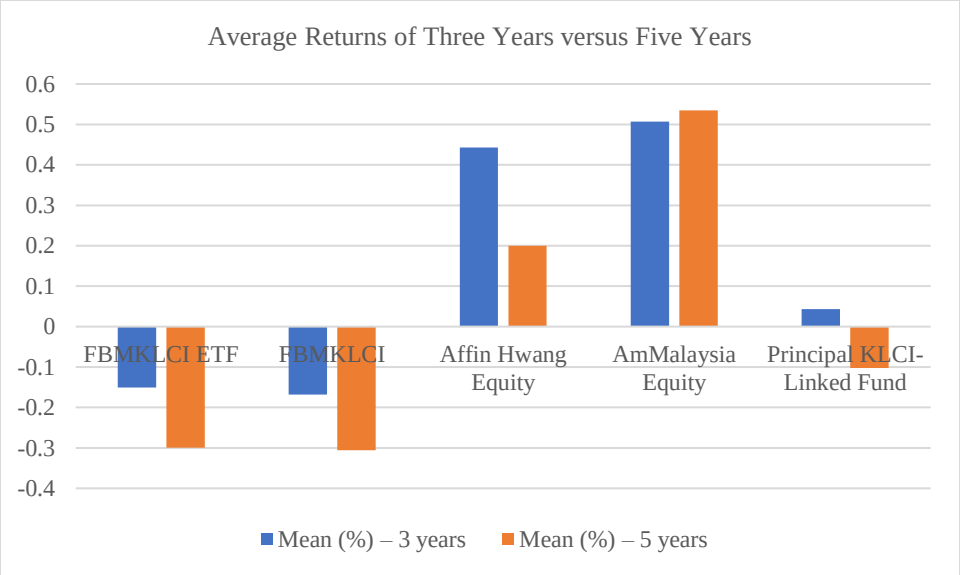

Figure 1: Average Returns of Three Years versus Five Years

Overall, the mean return has worsened over the five years for ETF, FBMKLCI, and Principal KLCI-Linked Fund. Although Affin Hwang Equity shows the same scenario, the fund manages to provide positive returns. The only fund that shows positive performance over the three-year and five-year period is AmMalaysia Equity. The mean return over the five years is slightly higher (0.5347%) than the three years (0.5073%). In brief, AmMalaysia Equity consistently shows positive returns. The returns even improved over five years, while the rest have seen their mean returns decline, with Principal KLCI-Linked Fund turning negative over the same period.

Table 4: Average Standard Deviation of Three Years versus Five Years

Funds	SD (%) – 3 years	SD (%) – 5 years
FBMKLCI ETF	4.1580	3.5989
FBMKLCI	4.2136	3.6727
Affin Hwang Equity	5.0942	4.1968
AmMalaysia Equity	5.5197	4.6229
Principal KLCI-Linked Fund	4.0605	3.5380

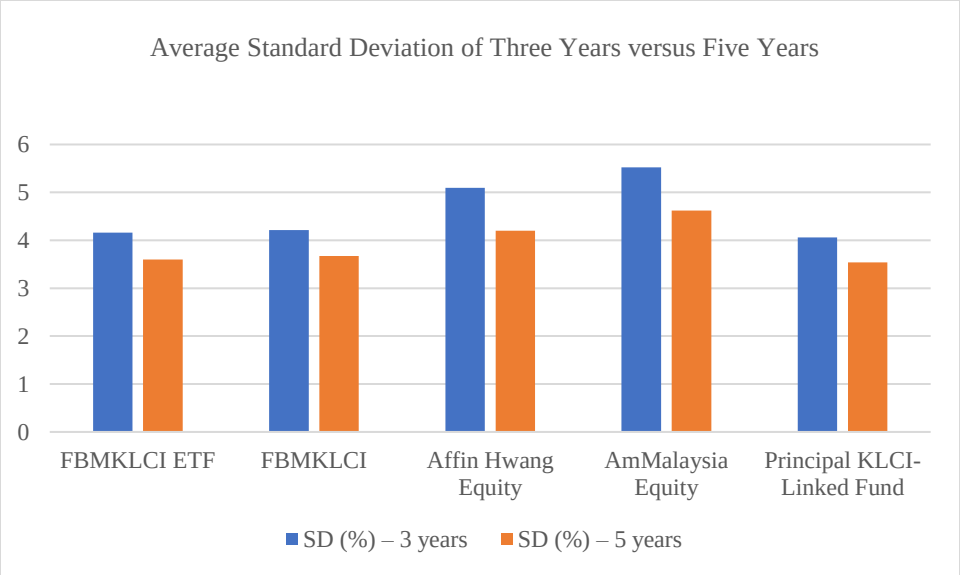

Figure 2: Average Standard Deviation of Three Years versus Five Years

Overall, the volatility of all funds is lower when observed for a more extended period. Thus, indicating a sense of security in the fund's stability in the long run.

Table 5: Average Beta of Three Years versus Five Years

Funds	Beta – 3 years	Beta – 5 years
FBMKLCI ETF	0.9731	0.9644
FBMKLCI	1.0000	1.0000
Affin Hwang Equity	0.9090	0.8490
AmMalaysia Equity	0.9787	0.8270
Principal KLCI-Linked Fund	0.9594	0.9588

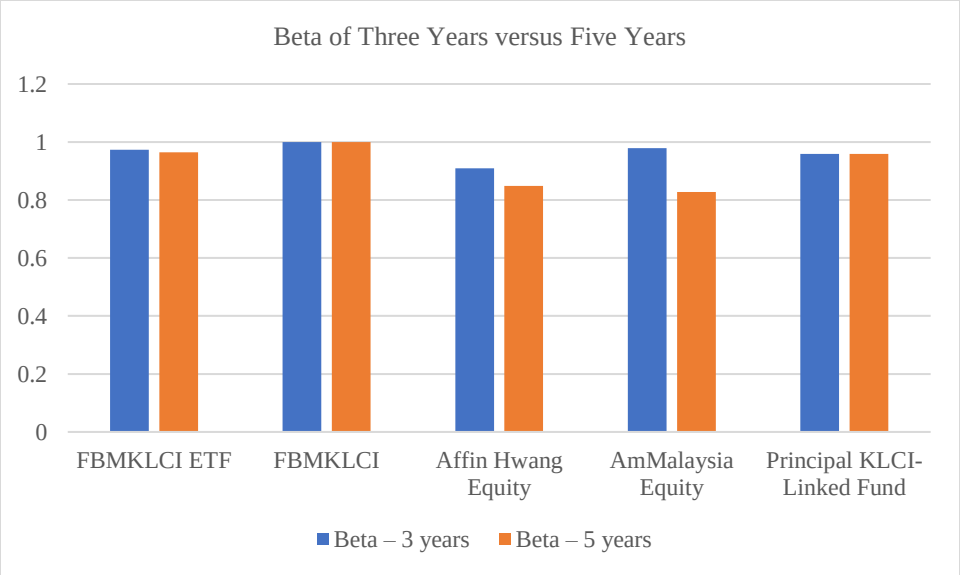

Figure 3: Average Beta of Three Years versus Five Years

All funds show slightly less volatility than the market over the five years.

Table 6: Sharpe Measures of Three Years versus Five Years

Funds	Sharpe Ratio – 3 years	Sharpe Ratio – 5 years
FBMKLCI ETF	0.0181	-0.0335
FBMKLCI	0.0138	-0.0347
Affin Hwang Equity	0.1313	0.0901
AmMalaysia Equity	0.1329	0.1543
Principal KLCI-Linked Fund	0.0662	0.0214

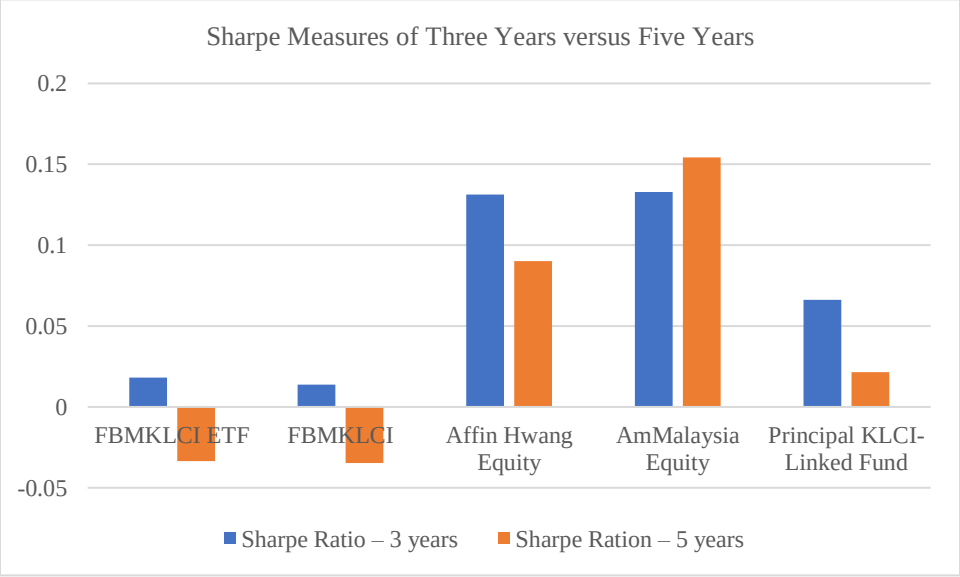

Figure 4: Sharpe Measures of Three Years versus Five Years

Table 6 and Figure 4 show that over the five-year period, all funds have worse risk-adjusted returns, with the exception of AmMalaysia Equity, which shows its risk-adjusted return is better over the five-year period than the three-year period. Nevertheless, the ranks of the funds are the same in both periods under study.

Table 7: Treynor Measures of Three Years versus Five Years

Funds	Treynor Ratio – 3 years	Treynor Ratio – 5 years
FBMKLCI ETF	0.0008	-0.0013
FBMKLCI	0.0006	-0.0013
Affin Hwang Equity	0.0074	0.0045
AmMalaysia Equity	0.0075	0.0086
Principal KLCI-Linked Fund	0.0028	0.0008

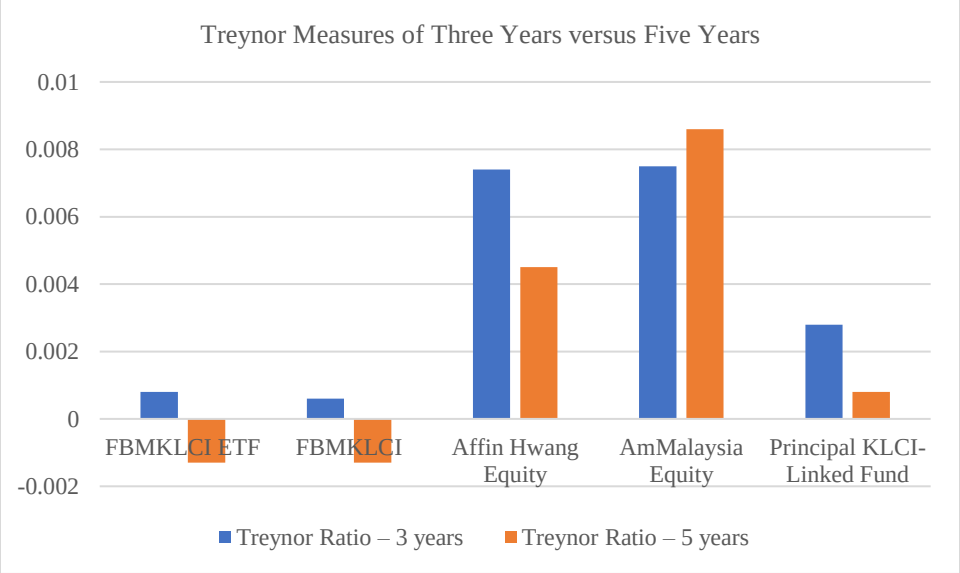

Figure 5: Treynor Measures of Three Years versus Five Years

Like Sharpe ratios, findings of Treynor ratios show that return per unit of market risk has worsened over the five years for all funds except for AmMalaysia Equity. Overall, findings indicate that the AmMalaysia Equity demonstrates the most consistent and positive trends, improving mean returns, risk-adjusted returns, and returns per unit of market risk. The other funds, particularly ETF and FBMKLCI, show a worsening trend in performance metrics over the extended period.

5.0 Conclusion

The advancement of financial technology has made it possible for the financial market to offer various investment options to investors. Among the popular choices are exchange-traded funds (ETFs) and unit trusts. While both investment vehicles have their merits, investors may face the dilemma of choosing between them. This study examines the performance of these two investment products over two specific periods, three years and five years. The results support the hypothesis that ETF and unit trust provide

different outcomes in terms of risk and return. Overall, findings for these periods show that unit trusts perform better. However, despite the performance disparity, the lower costs, flexibility, transparency, and strategic advantages of ETFs provide compelling reasons why ETFs should not be excluded entirely. In other words, ETFs offer a cost-effective, transparent, and flexible way to achieve diversification and meet specific investment goals. Therefore, including ETFs in an investment portfolio can provide long-term growth and stability, making them a worthwhile consideration despite their performance comparison to unit trusts.

Nevertheless, these results are not unexpected since ETF's performance tracks the performance of an index. It is worth noting that, unlike unit trusts, ETFs do not aim to beat the market. Investors investing in ETF should not base future performance on past performance. Furthermore, ETFs usually have lower management fees, typically below 1%. Whilst actively managed unit trust funds usually require higher management fees. In addition, there is also no sales charge imposed on ETF transactions like those incurred when investing in a unit trust fund. Typically, the upfront sales fee of unit trust transactions is between 3% and 5% of the total value. In conclusion, while ETF may not be the highest-performing fund in terms of annual return or risk-adjusted metrics, its characteristics and the inherent advantages of ETFs make it a compelling option for investors looking for a cost-effective, transparent, and flexible investment vehicle.

It is crucial to note the limitations of this study. This study uses a small sample set focusing on one equity ETF and three unit trusts. In addition to that, it is also limited to a relatively short period. Future studies may examine a more extended period, for example, 10 or 20 years. More studies should also comprehensively cover different types of ETFs and unit trusts. This study only focuses on equity funds. Therefore, the study does not conclusively show that investing in unit trusts is better than investing in ETFs, as an ETF’s investment objective differs significantly from that of a unit trust. In addition to that, given the rapid growth of passive investing, future studies should also look at the factors that impact the performance of these funds so that investors can make wise decisions among many alternatives available (Wu et al., 2020).

An important aspect that people often overlook is that both ETFs and unit trusts are merely vehicles for investing. The critical factor lies in the underlying securities held by these funds. All investment products come with varying degrees of risk, and it is inaccurate to claim that all ETFs are less risky than unit trust funds. Therefore, it is imperative to thoroughly understand the associated risks before investing in any product. In conclusion, there is no one-size-fits-all answer to the question of whether ETFs or unit trust funds are the superior choice.

When making this decision, it is prudent to consider one's personal preferences, risk tolerance, investment goals, and time horizon. Identifying the targeted expected return is essential to achieving financial objectives within the specified timeframe. Both options offer features that can align with preferences and are suitable, particularly for investors with a long-term horizon and a buy-and-hold strategy. Ultimately, the decision rests with the investor and should be based on risk tolerance and anticipated returns to choose the option that best aligns with the aimed financial goals.

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