“We feel allocation to funds with maturity of up to 3 years is a good option now”

By Anand Nevatia, Fund Manager, TRUST Asset Management Pvt. Ltd.

(**Anand** joined the Trading India chatroom on Refinitiv Messenger on the 20th of July ‘21 to discuss the Indian debt market. Below is his conversation with **Savio Shetty, Editor of Trading India**.)

Q: Let’s begin with why Trust MF felt the need to have a banking and PSU debt fund during these times?

A: We launched our Banking & PSU Debt Fund in January 2021 with a roll down strategy. There was a backdrop of multiple credit events and a very volatile interest rate environment. The yields in the money market are quite low whereas yields slightly beyond 3 years were giving a good spread and hence the launch of TRUSTMF Banking & PSU Debt Fund with a 3.5- year maturity.

Q: In the current scenario should a portfolio have more of private sector banks or public sector banks?

A: In regard to the debt instruments, the approach should be more from a perspective of how sound the bank is. The asset quality should be evaluated along with Capital Adequacy and ability of the bank to get in more capital as and when required. We have good banks both in public and private sector, so the choice should be bank specific and not just sector specific.

Q: Can you share more on the ACTIV methodology that Trust uses?

A: TRUST MF uses a trademarked ‘LimitedACTIV’ methodology to manage funds. The concept allows the fund manager to actively manage the funds within predefined limits. A model portfolio is created on the basis of the broad-based concept, post which limited deviations are allowed to the fund manager. These limits are primarily in respect to

a) The investible universe - This is a pre-filtered universe beyond which the fund manager cannot invest. the universe is periodically re-evaluated to include/exclude issuers based on pre-defined filters.

b) segmental allocation: there are ideal allocations with variance limits, which are not allowed to be breached.

This leads to the funds providing returns more commensurate to the underlying asset class.

Q: What are your views on Debt mutual funds having seen net outflows of ₹77,225 crore in the first half of calendar year 2021?

A: There has been a consensus view that we are at the bottom of the rates cycle and rates are likely to rise from here. The recent times have also seen lot of volatility in the interest rates. This period also witnessed the second wave during which enterprises were impacted for cash flows. We believe going ahead the flows are more likely to be concentrated towards the shorter end of the curve.

Q: What changes do you think investors should carry out in their allocation? Last year was excellent for debt funds.

A: We believe that the longer end of the curve will continue to be more volatile and that is the part of the curve which truly reflects the inflation expectations along with rate expectations. The shorter end of the curve is more driven by liquidity. While rates in the up to 1 year segment are rather unattractive, the 3-year segment continues to provide a good jump in yields. Further, this segment will also be impacted lesser as compared to the longer end as and when rates start to rise. We feel allocation to funds with maturity of up to 3 years is a good option right now.

Q: When do you think the spreads on PSU Bonds (over the G-Sec) would widen? Spreads have been compressed for a prolonged time. What do you think about the increase in issuances of Floating Rate Bonds (T-Bill Linked) by NBFCs? The levels have been rather very, very low. The rush to deploy has been imminent. Do you see adoption of Floaters on large scale?

A: The spreads on the longer end of the curve for AAA PSU bonds continue to be near historical averages. The spreads in the short to mid-term curve are compressed and is largely due to relatively lower issuances on this segment. This is currently one of the most active segments and we believe as and when more issuances come the spreads could start widening.
here have been a spurt of FRN issuances linked to T-bills more from NBFC issuers. The demand is also driven a lot from a spate of Floating Rate Funds launched recently. The demand for FRN is more from a perspective as investors look to hedge a rising rate scenario. The history of FRNs in India has not been very attractive. While they look attractive now, the liquidity is a concern and more importantly, the spreads on these notes can always widen in secondary markets.