Debt funds: What to expect in June

Dhawal Dalal of Edelweiss MF, Marzban Irani of LIC MF, Rajeev Radhakrishnan of SBI MF and Rahul Pal of Mahindra MF share their outlook on debt funds.

Bhakti Makwana & Sridhar Kumar Sahu 15 hours ago

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During May, yields on government bonds have settled lower due to excess liquidity, the surprise 40 bps rate cut by the RBI, wide spread risk-aversion mood and more importantly demand from banks for deployment of funds were raised.

Market participants also reacted positively to the government's Covid-19 related stimulus package of Rs.20 lakh crore after knowing that the package will not put a significant burden on the fiscal deficit of FY 2020-21. The balance sheet impact of the 20 lakh crore package is expected to be around Rs.2 lakh crore for the government, which is 1% of FY 2019-20 GDP.

Introduction of the new 10-year gilts also added to the positive sentiment and yields of old 10-year gilts declined by around 15 bps.

Corporate bonds witnessed brisk investment and trading in May amid investment demand from banks and mutual funds for high quality corporate bonds. The downtrend in yields was more pronounced in the short term AAA segment as steady appetite was witnessed from various participants.

WHAT TO EXPECT

Dhawal Dalal

CIO – Fixed Income
Edelweiss MF

- We expect incremental borrowing for FY21 in the 10-14 year segment largely through the new 10 year gilts
- RBI is probably at the end of its rate cutting cycle with one or two rate cuts left in FY21
- Based on that, we expect the short-end of the yield curve to remain attractive

Marzban Irani

CIO - Debt, LIC MF

- With reverse repo rate reduction, the excess liquidity is expected to come to the g-Sec market at the shorter end of the yield curve. Hence, the short end of the curve looks attractive
- On the longer end, with a huge weekly supply, ideally the yields should inch upwards
- However, with the regular intervention from the RBI, yields are expected to remain supportive

Rajeev Radhakrishnan

Head – Fixed Income
SBI MF

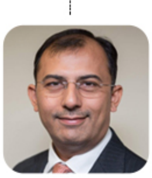
- Considering that the market appetite for non-banking financial corporation (NBFC) and housing finance company (HFC) has been largely restricted to specific names within the top rated spectrum, this would hinder access to a larger set of issuers
- The near term outlook on 10-yr g-sec would be shaped by the RBI and government providing clarity on funding of the additional market borrowings. In the absence of clarity, we expect a range bound market in the short term
- We remain fairly constructive on the medium term trend of 'low for longer' in terms of both policy rates and market interest rates
- This is conditional on the assumption that the excess borrowings would be absorbed either directly or indirectly by the RBI and or through a combination of other regulatory actions such as increase in held to maturity (HTM) limits etc

Rahul Pal

Head - Fixed Income,
Mahindra MF

- The caution for NBFCs will continue as participants would be vigilant on the credit costs rising due to the pandemic
- The near term outlook for gilts looks benign and steady
- However, as lockdown eases and with a bit of credit offtake as we move to the traditional busy season, gilt yields may inch up
- The short end of the yield curve would remain range bound with a softer bias, cushioned by liquidity and probability of further rate cuts

WHAT TO RECOMMEND



Dhawal Dalal

- In uncertain times like these, we advise to focus on fixed income funds with predominant

Marzban Irani

- In the current market scenario, with steepening of the yield curve expectations,

Rahul Pal

- Accrual strategies through low duration and short term plans
- Risk averse clients can

exposure to liquid and high quality credit

- Given a sharp decline in yields across the board, we believe that a combination of exposure to duration funds (35%), credit funds (15%) and short-term funds (50%) would be ideal at this point to capitalise from potential price appreciation as well as optimal yields for investment horizon of one year

investors may opt for 1-3 year period products like low duration and banking & PSU Fund depending on risk appetite of investors

look at PSU debt funds

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