

'Debt Markets Will Reasonably Outperform Gold & Commodities'

ET Q&A

AMIT TRIPATHI

CIO, FIXED INCOME INVESTMENTS,
RELIANCE MUTUAL FUND

For those of you who think there is no juice left in domestic debt market after a 125 bps rate cut in 2015, **Amit Tripathi** offers a corrective. He manages more than ₹1 lakh crore assets. The chief investment officer, fixed income investment of Reliance Mutual Fund spoke with ET's **Saikat Das**. Edited excerpts:

Will debt securities outperform this year?

Debt markets will reasonably outperform physical asset classes like gold and other commodities. As long as it is a short- to medium-term investment (2-3 years) a reasonable proportion needs to be invested in debt compared to equities. If you are talking about two-three years, from a moderate risk investor perspective, 40-60% of your allocations could go into debt. We are in an environment where rates have come down in the last 12-18 months. A pre-tax return in a range of 8% to 9% could be considered attractive from a debt investor's perspective. If the holding period exceeds 3 years, the post-tax returns look even better because of

indexation benefits.

What are the key positives for debt markets now?

Debt markets are reasonably well placed now. Positive real rates are the single biggest driver for investors and for markets to perform. Fundamentals continue to be supportive of debt markets. As long as fiscal discipline is maintained, debt markets will continue to do well.

Where should investors bet for?

The simplest product would be an FMP (fixed maturity plan) for three years. Even with AAA FMP portfolios, the investors can earn very attractive post-tax returns. For open-ended schemes, the dynamic bond category is an option if you are investing in a three-year period. Second is the corporate bond category. It can offer very attractive returns over a three-year period compared to other instruments like bank FDs or so. These returns are also tax efficient for investors.

Despite a 125 bps cut, Gsec yields

have not moved much in 2015. Are Gsec funds out of favour now?

We have to look at Gsec funds from a three-year perspective. Markets always tend to look ahead of actual rate cuts by the RBI. Long-term interest rates always react to macro fundamentals. A rally has partly happened over a three-year period. Second, markets also react to a lot of demand-supply, rather than acting purely to fundamentals.

Any reason for demand-supply mismatch?

Earlier between 2011-2014, we saw ₹70,000 to ₹1,00,000 crore worth of additional demand in the market either due to the RBI OMO (open market operation) or FII demand. 2015 was the first year when FIIs were not there as they exhausted their limits mostly.

The RBI, too, did not do OMO purchases; they did OMO sales between April and September this year. So, you suddenly have a demand-supply situation which is different compared to the last three years. That is also a reason, on the immediate basis, why markets did not rally.

How does an investor gain from the divergence between short and long term rates?

If you see an overnight rate of 6.75% and then consider the benchmark 10-year rate of 7.75%, you have seldom seen such spreads in a rate-cutting cycle. So, it is an attractive entry point for investors from that perspective. In the short-run demand supply will outweigh this attractiveness, and hence, investors need to come with a two-three year perspective. I am sure that two-three perspective debt fund returns will remain attractive in the overall scheme of things including dynamic and gilt funds.

Any piece of advice for short-term debt investors?

If your investment horizon is less than a year with some risk appetite, you can look at a government securities fund. For an investor with an even shorter horizon of three-six months, they could look at an aggressive ultra short-term fund which run a duration of one to 1.5 years.

For investors with a three-six month time horizon, ultra short-term funds,

which have a maturity profile of around 1 year, are most suitable, as they provide a combination of roll-down and capital gains benefit. The investors can generate returns reasonably in excess of liquid funds. For investors who have a risk appetite and a one-year time horizon, some tactical allocation can be made to gilt funds given the current attractive valuations.

What is your call on domestic rates this year?

Our sense is, we see headroom for another 25-50 bps rate cuts in 2016. Demand-supply (of papers) situation would be much better in the markets. Macro fundamentals will continue to remain attractive.

Will Fed rate hikes, expected this year, lead to overseas fund exits?

The spread between India (bond yields) and developed markets has widened significantly. For example, from an average of 300-350 bps spread between India and US benchmark yields, the spread has increased to almost 700 bps in 2013. From there, now it has come down to about 550 bps. But, we are still

much higher than the level we had seen in the last decade between 2002-2010.

If fiscal discipline, consumer price inflation and current account stay stable, you will see the gap between India and developed market rates coming down further. For foreign investors, a stable currency is an important reason for Indian markets to remain attractive especially on the debt side. You put money on debt for stability, not for growth.

A 8% rate with a stable currency is an attractive proposition for overseas investors. If US Fed hikes rates by as much as 25-50 bps this year, it will have a short-term impact, but India will continue to remain insulated as far as our domestic macro remains stable. We need not worry that much as long as our macro remains stable.



COMPANY PHOTO



Our sense is, we see headroom for another 25-50 bps rate cut in 2016. Demand-supply (of papers) situation would be much better in the markets