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Gilt funds returns outshine other debt categories'

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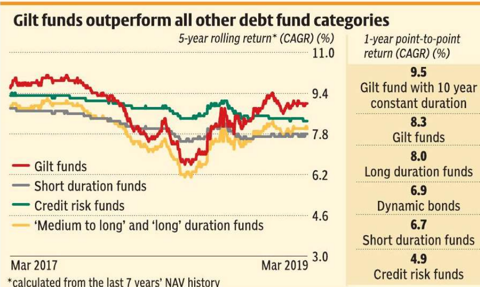
Gilt funds have given an annualised return of 8.3 per cent over the past year, outperforming all other debt fund categories. Top Gilt funds have delivered returns as high as 11 per cent.

Other debt funds that invest in corporate bonds (including long-, low- and short-duration, and credit risk funds) delivered annualised returns ranging from 4.9 per cent to 8 per cent in the same period.

Gilt funds invest mainly in government securities of varying maturities. While they carry no credit risk, they are exposed to interest rate risk. They generate higher returns when interest rates are falling and lower or negative returns when interest rates rise. In the short run, the returns are volatile.

Swing in returns

Gilt funds delivered a muted performance in 2017 and the first half of 2018. Concerns over inflation, tightening global liquidity, and the RBI hiking its key repo rate pushed up bond yields and, in turn, impacted the NAVs (net asset values) of all debt funds (if rates move up, bond prices fall, and vice-versa).



But conditions have been improvung for these funds. "Over the past six months, with structural improvements in inflation, the focus has shifted to improving growth," said Prashant Pimple, Senior Fund Manager, Reliance Mutual Fund. "So interest rates moved lower and delivered higher returns for duration funds (funds that churn their portfolio based on the interest movement)."

"Gilt funds have performed well due to the coupon earned, minimal changes in point-to-point 10-year G-sec yields, and timely adjustments of the portfolio based on the rate movement," observed Deepak Jasani, Head - Retail Research at HDFC Securities. "Non-Gilt debt funds, however, were unable to benefit to the same extent as the spreads of corporate paper did not narrow as interest rates softened and also because the value of some papers, whose ratings were downgraded, had to be written down."

Bet for the long term?

Given their allocation to sovereign bonds, Gilt funds are viewed as a safer investment option, especially in a scenario where debt funds , including liquid ones, are haunted by the spectre of bond defaults and credit rating downgrades.

Over a longer period, too, gild funds have fared better. The five-year rolling returns of gilt funds for the past seven years have been higher than that of other debt fund categories.

"For investors looking for a long time-frame, Gilt funds should indeed be a part of their portfolio. However, the selection of the Gilt fund is crucial, as not all have done well," said HDFC Securities' Jasani. His tip: Spread the entry time over four-six months.

"Past returns have absolutely no bearing on future performance, especially when it comes to Gilt funds," cautioned Ashish Shanker, Head of Investment Advisory, Motilal Oswal Private Wealth Management.

Constant maturity funds

Interestingly, the recently launched innovative category — Gilt fund with 10-year constant duration — delivered 9.5 per cent annualised returns over the past year and outpaced the general Gilt funds category.

"Normal Gilt funds are a better option than constant maturity Gilt funds as duration management plays an important role in delivering superior returns over the medium to long term. Normal Gilt funds allow fund managers to execute his views across different maturities of G-secs across yield curve, whereas in constant maturity Gilt funds, they have to stick to a particular maturity," pointed out Reliance MF's Pimple.