

investing

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“Both high grade and high yield funds look attractive”

Interest rates are likely to remain range-bound, making both ultra-short and short-term schemes, and credit risk funds with 1-3 year duration quite attractive, Amit Tripathi tells **Sanket Dhanorkar**



Amit Tripathi,
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Is the fragility in the bond market likely to stay for a while?

We have already seen the bulk of the yield movement in the past 18 months, and it is likely to be range-bound (7.5-8%), till the macro picture—external and domestic—becomes clear. There has been an uptick in spreads in the recent past, driven primarily by liquidity conditions. While high grade spreads look attractive, the financial sector spreads will remain elevated for some time, owing to asset liability management (ALM)-driven issuance pressures.

Are NBFCs equipped to overcome the current hardships?

NBFCs have been there for long and are well-equipped to handle liquidity and credit cycles. The sector is also quite diverse, from pure retail to pure wholesale lenders, each with a different asset and liability side construct. The environment calls for consolidation in terms of growth, ALM, asset

quality and leverage, and most of the NBFCs are fully aware and capable of adapting. In fact, once the dust settles, we may see some NBFCs taking advantage of market dislocations to capture higher market share.

How big are concerns over the fall in rupee and rise in oil prices for the bond market?

Oil and rupee are both a current account and an inflation play, so any marked movement needs the market to adjust. The market has broadly adjusted to the recent move in oil and rupee, and has factored in the medium-term impact on inflation as well. However, any sharp move from here on may result in another round of adjustments. The good news is on the inflation front, which, in spite of challenges of the post-GST environment, adverse oil and currency movement, has still remained below expectations, led by very soft food inflation, and controlled core inflation.

How would you assess the credit health of Indian companies?

The private sector has broadly deleveraged over the past five years, the balance sheets look better, and the operating leverage is helping. The financial services space is generally well capitalised, barring some names, but the asset-side issues will have to be monitored in the near-to-medium term. But we strongly believe in a bottom up approach to credit. A generalist sectoral approach doesn't work well when there are noticeable distinctions in terms of management quality, information asymmetry, and a dynamic business environment.

At a time when the reliability of credit ratings is under question, can bond funds do better credit appraisal?

Credit appraisal is a detailed, intensive process; very bottom up in nature, calling for the right blend of quantitative and qualitative inputs. The very fact that fund managers have a choice to exercise (the ability to say no to rating agencies), means they can do a better job, as long as their analysis is thorough, forward looking through the cycle. Our own track record specifically, and the fund industry's track record in general, has been a testimony to this. As portfolio managers, we have a fiduciary responsibility in terms of our investor mandates. We have to be convinced fully in terms of the issuer, security, structure and credit performance before we commit to any investment. It is backed by a rigorous and quality process and

people infrastructure.

How long is the interest rate upcycle likely to last this time?

The RBI is clearly focused on inflation as the key driver for their policy—interest rate and liquidity—decisions. Given the current and expected trajectory of inflation—our estimates for 2018-19 and 2019-20 are comfortably in the RBI 4% (+/-2%) range—going forward we don't envisage more than one or two rate hikes. Given that markets have already priced in a bulk of this move, we don't see rates rising beyond the recent highs over the next 6-12 months. The risk to our view can come from loose local or global fiscal policies, which can have a negative impact on the inflation trajectory.

What type of bond funds make most sense for investors now?

Given the fact that a large part of the interest rate move has happened, bond funds across categories look attractive from a one-to-three-year time frame. However, we are still some way away from any secular downward move in rates, given the evolving local and global macro trends.

In this environment of range-bound rates and attractive carry, investors could choose from high grade (ultra short-term and short-term funds) or high yield (credit risk) funds which operate with a 1-3 year neutral duration strategy. In the near future, carry will be the predominant driver of returns in the fixed income category. Duration funds can be a tactical play for now, till such time there is clarity on the macro environment.

Have the revised scheme categorisation norms for bond funds impacted fund managers? Are investors better off under the new structure?

The scheme recategorisation has provided much-needed clarity in terms of interest rate and credit risk that various categories of funds carry. It also makes life easier for investors to compare funds in the same category and take informed decisions based on their risk-return profile. From our perspective, given that we have always adhered to fund positioning in letter and spirit, the formal fund categorisation reinforces our stand of being true-to-label.

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