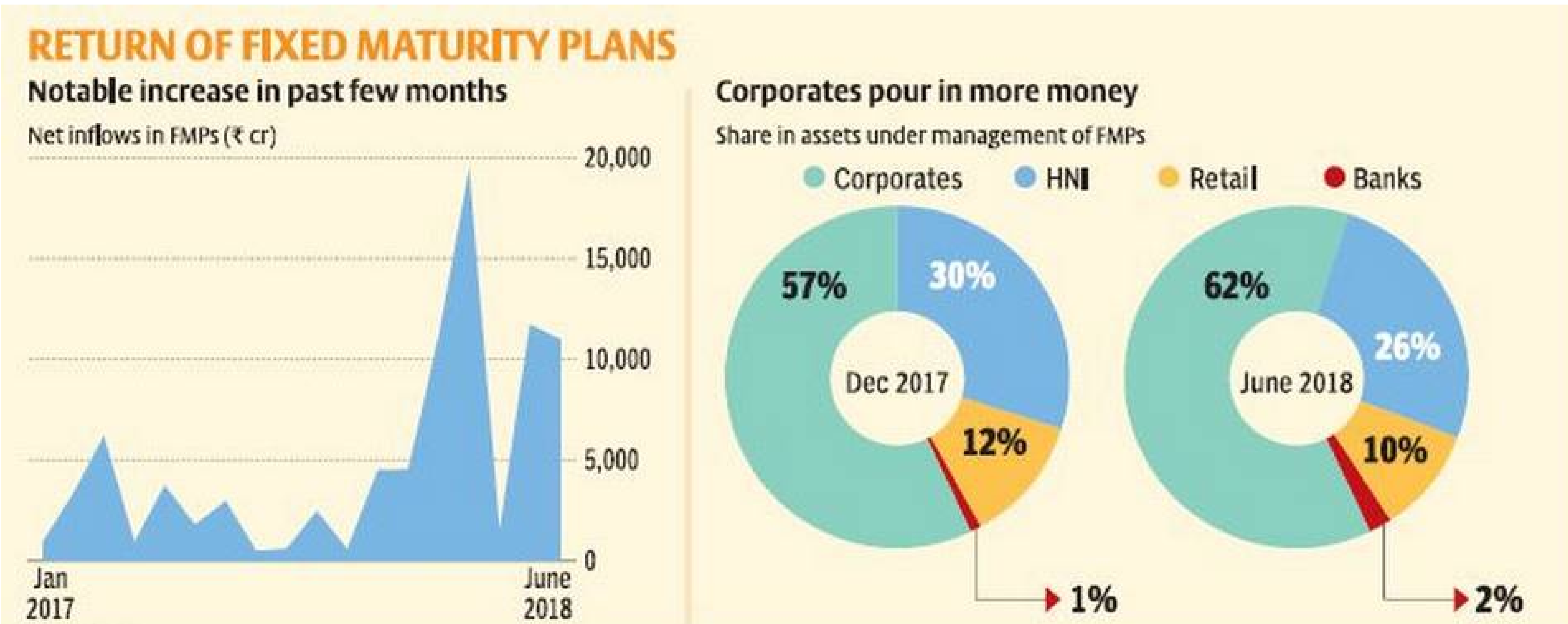
Bond effect: Fixed Maturity Plans on a high

DHURAIVEL GUNASEKARAN



Source: AMFI

Rising bond yields, indexation benefit have made the debt funds attractive for investors

BL RESEARCH BUREAU

Fixed Maturity Plans (FMPs) within the debt fund category are the flavour of the season for institutional investors.

Out of favour last year, FMPs have recorded significant inflows the past few months, thanks to the prevailing high bond yields that have raised the interest of the institutional investors.

Data sourced from the Association of Mutual Funds in India (AMFI) show that the monthly net inflows into FMPs, which ranged from ₹1,000 crore to ₹3,000 crore last year, shot up sharply in 2018. The inflows were notably high in May and June, at ₹11,711 crore and ₹10,991 crore, respectively.

FMPs are close-ended mutual funds that one can invest in only during a New Fund Offer. As FMPs invest in debt instruments that have the same maturity as that of the fund, they are free from interest rate risks. But they do carry a credit risk, as there is the possibility of default by the debt issuing company.

Until 2014, when the Budget delivered a severe blow to FMPs, these funds enjoyed great tax advantage. Earlier, gains made on debt funds held for more than one year were treated as long-term capital gains (LTCG) and taxed at 10 per cent flat. Fund houses issued FMPs for slightly more than one year so that investors could enjoy lower LTCG.

But, in 2014, the tenure to claim LTCG on debt funds was raised to three years, and this came as a major setback to FMPs. Further, a notable fall in returns in the past two years left little on the table for investors.

But the rise in corporate bond yields in the past few months has rekindled investor interest.

A Balasubramanian, CEO, Aditya Birla Sun Life AMC, says: "Bond market yields have been rising over six-eight months. Along with sovereign yields, corporate bond yields across rating profiles have also inched up. The general expectation is that the RBI will further hike interest rates in the year ahead. So, on an absolute basis, corporate bond yields are trading at attractive levels."

Three-year AAA-rated bonds are trading at around 8.65 per cent and AA-rated corporate bonds at 9.11 per cent, giving investors a chance to lock in their investments to benefit from these high yields, adds Balasubramanian.

From the tax perspective, too, FMPs are attractive if investments are held for at least three years to get the LTCG benefit, which is levied at 20 per cent with indexation. The indexation benefit allows the investor to index his investment to inflation, which minimises the tax outgo considerably. To retain the double indexation benefit (if invested towards the end of the financial year), fund houses launch FMPs with a tenure of more than three years.

Dwijendra Srivastava, Chief Investment Officer (Debt) at Sundaram Mutual Fund, explains that the three-year AAA rates, north of 8 per cent, offer a compelling tax-adjusted return compared to a tax-free bond of the same maturity due to the indexation benefit.

FMPs saw significant inflows the last couple of months on account of the uncertain interest rate environment, he observes. “Even open-ended funds on the money market spectrum are witnessing volatility. This has prompted investors to go for close-ended fixed income schemes, where returns are more predictable,” he adds.

Surge in corporate flows

Over the past six months, FMPs attracted total net inflows of ₹59,226 crore. AMFI data show that corporates, in particular, have poured more money into FMPs. The share of corporates in FMPs’ assets under management increased by 5 percentage points over the past six months — from 57 per cent as of December 2017 to 62 per cent as of June 2018. While the share of retail and HNI investors dropped in absolute terms, their corpus in FMPs rose 15 and 18 per cent, respectively, over the same period.

Published on July 22, 2018

TOPICS money and investing government bonds

RELATED

10-year bond yield hits 2-month low

India's 10-year bond yield today hit a 2-month low on surprise open market ...

Previous Story
Scent of Tiger in the air as wind picks up at Carnoustie

Next Story
Five things to watch out for on July 23

Email

Subscribe

More From The Hindu Business Line

Ashok Leyland shares slump 14%

YES Bank (Buy)

Top bankers welcome move

HDFC AMC sets IPO price band at Rs 1,095-1,100

SBI to enter digital lending space in a big way

Truecaller acquires Chillr to start mobile payments services

A man who nurses banks back to health

Canara Bank launches RuPay credit card

RBI’s Institute offers PG diploma in banking tech

MORE FROM BUSINESSLINE

What ails small- and mid-cap stocks

Analysts cite SEBI move on restructuring MF plans, ASM, physical delivery in F&O as reasons

Rahul hugs Modi: Twitter abuzz with jokes on ‘hugplomacy’, ‘pappukijhappi’

Congress chief Rahul Gandhi’s surprise gesture to hug Prime Minister Narendra Modi in the Lok Sabha after his speech during the no-confidence debate had Twitter abuzz today with jokes aplenty and the

Walmart Foundation invests $2 million in Icrisat project

Walmart Foundation has invested $2 million in an Icrisat project to support 6,000 small farmers in Andhra Pradesh. The project is aimed at improving their business model to realise better value chain

1. Comments will be moderated by The Hindu Business Line editorial team.

2. Comments that are abusive, personal, incendiary or irrelevant cannot be published.
3. Please write complete sentences. Do not type comments in all capital letters, or in all lower case letters, or using abbreviated text. (example: u cannot substitute for you, d is not 'the', n is not 'and').
4. We may remove hyperlinks within comments.
5. Please use a genuine email ID and provide your name, to avoid rejection.