Fed rate hike queers pitch for debt mutual funds

BY SHIVANI BAZAZ, ECONOMICTIMES.COM | UPDATED: JUN 15, 2017, 05.35 PM IST

Many money market pundits were hopeful of a rate cut by Reserve Bank of India (RBI) in the coming months after retail inflation hit 5-year low recently, but US Federal Reserve's second interest rate hike this year has queered the pitch. A section of money market participants believe RBI may become cautious and delay rate cuts, while some believe that the central bank may go by the numbers and ease rates if numbers support it. Against this backdrop, what should be your debt mutual fund strategy?

"This is negative for Indian debt markets, as the fed rate hike will make it difficult for the RBI to cut rates. The RBI was dovish and there were signs of a rate cut in the coming quarter because of the strong domestic numbers. But if the global scenario is not favourable, it will be difficult for the RBI to cut rates," says Mahendra Jajoo, Head of Fixed Income, Mirrae Asset MF.

Many experts share Jajoo's view that the rate hike is likely to impact the global liquidity which has been the driving force behind emerging markets rally. India is also riding the wave on the back of global inflows. However, emerging markets did not lose much ground in early trade today. That is why a section of money market believes that RBI may proceed as per plans if numbers are good, the banking regulator would cut rates in the coming months.

"The Fed rate hike was on expected lines, this is just the second hike of the four that they spoke about earlier. This is pretty much consistent and thus it hasn't surprised anyone. I think the impact on the local fundamentals is very limited," says Kumaresh Ramakrishanan, Head - Fixed Income, DHFL Pramerica Mutual Fund.

"I don't think this hike will have a major impact on the future course of rate cuts by the RBI. The domestic fundamentals and data is strong and I think RBI's next decision will be based on how the numbers of July come out to be," he adds. However, he is quick to add that it is not possible to predict when exactly the rate cuts would take place.

Debt mutual fund strategy

Jajoo says he has been repeatedly speaking about the importance of dynamic bond funds in such a juncture in the market. "In the last three months they have given 15 per cent returns. We are at a point where the expectations are changing regularly from a rate cut to a no change to a rate hike. For investors with a three-year or above horizon, I think dynamic bond funds are the best option," he says.

Ramakrishnan of Pramerica Mutual Fund says, "we are suggesting the short and medium-term funds. I think the medium-term segment is very attractive."

However, both fund managers believe that long-term debt mutual fund investors should not change their strategy now. "Investors who are invested in long-term funds do not need to cut the exposure or move out. We are not sure about anything at this point. I think investors should take a call once the picture is clear," says Jajoo.

"The long-term investors shouldn't be changing their stance right now. It makes sense to have duration in your portfolio at this point in time. And also we are not sure if there will or will not be a rate cut, we can only speculate. So staying put in your long-term funds makes sense," says Kumaresh Ramakrishanan.

Debt funds recommended by mutual fund advisors

Neeraj Chauhan, CEO, The Financial Mall
Dynamic Bond Funds : ICICI Prudential Long Term Fund

Vishal Dhawan, Founder & CEO, Plan Ahead Wealth Advisors
Short-term debt schemes: Birla Sun Life Short Term Fund
Medium Term debt schemes: HDFC Medium Term Opportunities Fund
Dynamic bond schemes: Birla Sun Life Dynamic Bond Fund, IDFC Dynamic Bond Fund