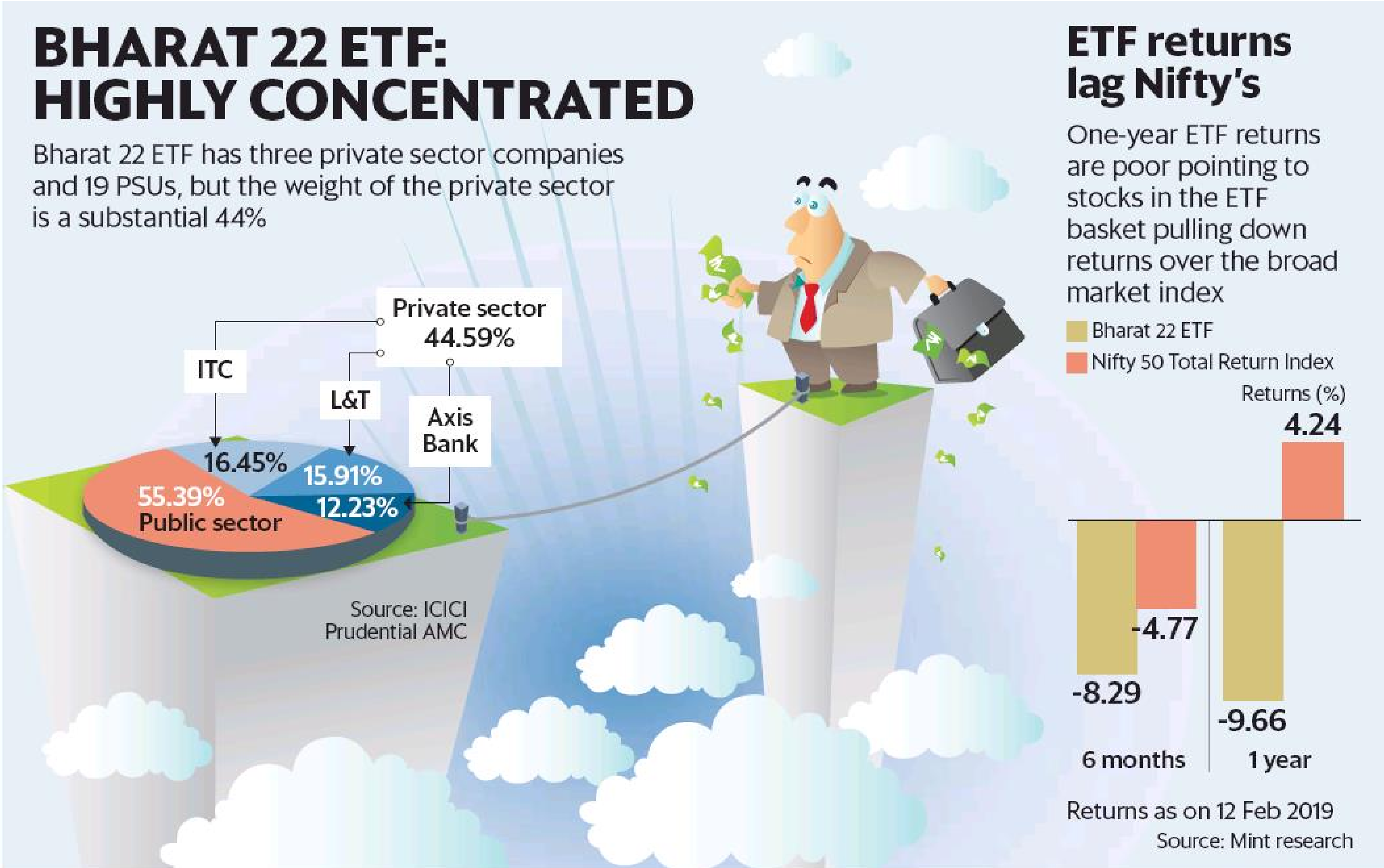
Neil Borate
neil.borate@htlive.com



SANTOSH SHARMA/MINT

The Bharat 22 ETF (exchange-traded fund) has opened a window to allow in new investors on 14 February 2019. The ETF tracks the Bharat 22 Index which comprises 22 companies—19 public sector companies or PSUs and three private sector firms.

The government of India plans to raise an additional ₹3,500 crore through this additional offering managed by ICICI Prudential Asset Management Co. Ltd. Investors who subscribe to this additional offering will get a 5% discount on the reference price, which is the volume weighted average price of its constituents on the offer date.

WHAT IS BHARAT 22 ETF?

Bharat 22 ETF is the result of a historic accident. Financial problems and mismanagement in the erstwhile Unit Trust of India (UTI) forced the then government to carve out a special component of UTI called the Specified Undertaking of the UTI (SUUTI) and transfer several UTI holdings into it. In Budget 2017, the government announced its intention of creating an ETF to sell off the holdings in SUUTI to raise revenue. This led to there is no sound investment logic stitching this ETF together, other than the government's need to disinvest and, hence, it's difficult to recommend it for the long term. "Bharat 22 is good from the government's point of view but not from an investor's point of view. It is simply the result of the disinvestment needs of the government and has no clear cut investment rationale anced according to the government's divestment needs.

But what about bluechips in the ETF like Axis Bank Ltd, Larsen & Toubro Ltd and ITC Ltd? Won't these pull up returns? Investors can directly buy these stocks without having to go through an ETF. Alternatively, they can take exposure through a mutual fund. Bundling these bluechips with poten- ETF is suitable for investors who can take higher risk because its portfolio is quite concentrated.

But what about the discount? Is that not a good enough reason to invest? "The 5% discount looks attractive but investors should also note the poor returns delivered by the fund in the past. Investors who have a high level of confidence in PSUs should consider investing in

SUUTI to raise revenue. This led to the creation of the Bharat 22 ETF.

As mentioned earlier, the ETF has 22 companies, out of which 19 are PSUs. However, in terms of weight, the three private sector companies account for a significant 44% portion of the ETF with the balance 56% in PSUs (*see graph*).

SHOULD YOU INVEST?

Bharat 22 ETF has lost 8.51% since its launch on 17 November 2017 till date. So, ₹100 invested in November 2017 is now worth ₹91.49.

After collecting ₹14,500 crore in the new fund offer in 2017, the ETF had opened another subscription window in June 2018 and collected ₹8,400 crore. The assets under management of the ETF have now plunged to ₹5,179 crore, barely a fourth of what was collected in 2017 and 2018. The reason why investors have lost interest in the ETF has been poor performance (*see graph*).

Unlike a diversified mutual fund, no clear cut investment rationale. We would not recommend it to our clients," said Suresh Sadagopan, founder, Ladder7 Financial Advisories.

However, according to S. Naren, chief investment officer, ICICI Prudential AMC, the product is suitable for long-term investors to partake in the India growth story. "The constituents of ICICI Prudential-managed Bharat 22 ETFs are available at very attractive valuations given their lower P/E and offer relatively better earnings growth and higher dividend yield in comparison to Nifty 50/S&P BSE Sensex," he said.

But investors should note that since Bharat 22 ETF has been created to service the government's disinvestment programme rather than for investment needs, its portfolio runs the risk of being rebalding these bluechips with potentially underperforming PSUs can drag down returns.

Bharat 22 ETF's portfolio runs the risk of being rebalanced according to the government's divestment needs

Financial advisors pointed out the risks of concentration with the three bluechip stocks.

"We think that the concentrated positions in the three private sector bluechips, especially L&T and ITC, make it a fairly concentrated ETF which enhances risks for investors looking at truly diversified portfolios. We believe investors are better off looking at more diversified ETFs based on the Nifty and Nifty Next 50 with low expense ratios and low tracking errors against their respective indices," said Vishal Dhawan, founder and CEO, Plan Ahead Wealth Advisors Pvt. Ltd.

Mrin Agarwal, founder-director of Finsafe India Pvt. Ltd, said the PSUs should consider investing in it," said Deepak Khemani, a Mumbai-based wealth manager. Investing for the discount, typically, means exiting immediately after getting allotment. This is a risky but potentially profitable short-term trade, and not something we recommend our readers do.

But long-term investors have no such reason to invest. "We normally see hot money coming into this ETF for the discount offered. Also, a lot of funds do hedging of their allocation in futures to use this arbitrage opportunity. For retail investors with a 5% discount, the downside is protected for listing gains. But in the long term, this has underperformed large-cap funds and the index. Hence it is better to avoid this for the long term," said Lovaii Navlakhi, founder and CEO, International Money Matters Pvt. Ltd, an investment advisory firm.

Serious long-term investors have no reason to invest into this ETF.