



Ajit Menon
CEO

A Win-Win Solution

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"That's been one of my mantras – focus and simplicity. Simple can be harder than Complex"

– Steve Jobs

Dear Investors and Partners,

Although retail participation in mutual funds, has grown by leaps and bounds in the last two decades, it is predominantly equity schemes that investors have favoured. As per AMFI data as of Jan-23, individual mutual fund investors have 80% of their total mutual fund allocation towards equity schemes and only 14% of the allocation is towards debt-oriented schemes.

Hitherto, competition from traditional, guaranteed fixed income products have meant that Indian investors were not really worried about the accrual interest income bit in their portfolios. On the other hand, the potential to earn alpha in a debt asset class through active management – whether through exposure towards relatively lower credit ratings or through active interest rate management – was something a retail investor didn't understand due to its seeming complexity. This has meant that they haven't participated in this particular asset class in any meaningful manner. However, awareness around this is slowly changing for two reasons. Firstly, investors are learning to evaluate their traditional debt investments through the lens of inflation-adjusted returns. Secondly, they are considering post-tax returns. On both these counts, traditional products may not deliver. However, investors still take comfort from the visibility of future returns that these traditional investments offer. In recent years, an interesting development in the form of passive debt mutual fund, popularly known as Target Maturity Fund (TMF), however looks to bridge this gap and perhaps create a win-win situation for all stakeholders. Till last year, the TMF category and even the traditional debt products weren't too attractive for investors, because of low interest rates prevailing in the economy. However, globally and in India too, the central banks have raised rates and the yields on such products on an absolute basis is now attractive. In this backdrop, a TMF with portfolio comprising of only G-Secs may seem like a panacea. Let me explain how.

The prevailing yield minus the expenses is approximately what the investor can expect to earn at the end of the tenure, under normal circumstances. However, this return can be lower if there is any downgrade or default in any of the papers that the scheme may be holding. This is where a G-Sec only portfolio can provide greater comfort to the investor in India (who is very risk averse when it comes to debt investing). A TMF is also tax-efficient for investment horizon greater than 3 years, due to indexation benefit, unlike traditional debt instruments. Investors can adjust cost of acquisition with inflation (CII Index) while calculating capital gains on the same. Thirdly, if investors can hold the TMF till maturity, then any interim volatility in terms of interest rate movement will not matter. For e.g., if the interest rate starts to rise, an investor in an active debt mutual fund scheme may face capital loss. Similarly, a TMF's NAV may also be affected. However, as the TMF approaches maturity the NAV is expected to gradually reflect the par value. This is commonly known as roll-down of security. Another important point missed by most advisors and investors is the tenure. TMFs nowadays are available for various maturities, and as far out as 15-20 years and longer. This may eliminate re-investment risk as well. On the other hand, traditional debt instruments rarely provide locking-in of interest rates for such longer tenure. As a result, investors may or may not get the same levels of yields at the time of roll over.

Thus, a G-Sec only TMF takes care of investor preference in India for safety-first. Such a debt product has minimum credit risk, as it is backed by government securities and has sovereign rating. This helps investors as a simple choice, with its single point portfolio focus and advisor or investor need not track too many things.

Secondly, a GSec only product, is a smart alternative, both from taxation and returns aspects. Lastly, it provides for asset allocation planning for the longer term. All this at a relatively lower level of expenses. Keeping this thought process in mind, we at PGIM India have recently launched a G-Sec only product (PGIM India CRISIL IBX Gilt Index – Apr 2028 Fund).

Thank you for your continued trust and confidence in our investment management services. If you have any questions or concerns, please do not hesitate to reach out to PGIM India team or our distributor partners as well.

Stay safe & happy investing.

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Mutual Fund Investments are subject to market risks, read all scheme related documents carefully.

PGIM India CRISIL IBX Gilt Index - Apr 2028 Fund
(An open-ended Target Maturity Index Fund investing in constituents of the CRISIL-IBX Gilt Index - April 2028. A relatively high interest rate risk and relatively low credit risk)

This product is suitable for investors who are seeking*:

- Income over the target maturity period
- An open-ended Target Maturity Index Fund investing in constituents of the CRISIL-IBX Gilt Index - April 2028
- Degree of risk – MODERATE



Investors understand that their principal will be at moderate risk

* Investors should consult their financial advisors if in doubt about whether the product is suitable for them.