

Debt funds may benefit if HNIs shift from MLDs

SIDDHANT MISHRA
Mumbai, February 7

FINANCE MINISTER NIRMALA

Sitharaman's proposal to tax gains from market-linked debentures has put the spotlight on HNI investors and a potential shift in their investment strategy.

Market-linked debentures (MLDs) are a ₹15,000-crore market annually, which is relatively quite small in comparison to over ₹6.5 trillion of premium mobilisation in life insurance, ₹1.5 trillion mobilisation in SIPs and ₹30,000 crore of mop-up in the PMS market.

In her Budget speech, the finance minister proposed to tax gains from MLDs as short-term capital gains. Experts say debt funds could benefit and see an increase in inflows as there may be a shift in the HNI (high net worth individual) money.

Data from Prime Database show that the total issuance up to January this year by the top five issuers stood at ₹2,233 crore. The same for 2020 was at ₹12,103 crore, while for 2021 and 2022, the figures saw a jump, recording ₹24,611 crore and ₹22,797 crore, respectively.

Divam Sharma, founder of Green Portfolio PMS, said HNIs are bound to shift their allocation to products that give higher returns and attract lower taxation — debt mutual funds and bonds.

"The recent rise in interest rates have made debt funds more attractive. Since the MLD market is still evolving, taxation and the quantum of returns are the important factors.

Also, the bond market is evolving and with the recent Sebi guidelines around this product, there are opportunities to generate returns of 7-13%, with a minimum investment ticket size of ₹1 lakh from investing in bonds of banks and NBFCs," he added.

Anil Rego, founder and fund manager at Right Horizons PMS, says while MLDs' ability to deliver up to 8.0-8.5% post-tax returns made them attractive, one could now consider debt MFs (holding for 36+ months), venture capital debt and REITs for better post-tax returns.

"VC debt could deliver 12% pre-tax returns and REITs generally deliver 12-14% pre-tax returns at an equal or higher risk," he said.

AT-1 bonds of larger banks, AIFs, and structured products are also options but he pointed out that one should be fully aware of the risks associated. For those with a moderate risk appetite, dynamic asset allocation funds makes sense, he added.

But better returns could be the more important goal, given the higher expected tax incidence.

Abhijit Bhawe, CEO of Fisdome



NUMBERS SAY IT ALL

2021

| | |
|-------------------------------|--------|
| Summit Digital Infrastructure | 11,836 |
| HDFC | 5,000 |
| Shriram Finance | 3,287 |
| REC | 2,500 |
| Shriram City Union Finance | 1,988 |

2022

| | |
|----------------------------|--------|
| DME Development | 10,000 |
| Anand Rathi Global Finance | 3,868 |
| Bharti Telecom | 3,800 |
| Nuvama Wealth & Investment | 2,652 |
| API Holdings | 2,478 |

2023 (January)

| | |
|----------------------------|-----|
| Anand Rathi Global Finance | 638 |
| Piramal Enterprises | 500 |
| Nuvama Wealth & Investment | 470 |
| ECAP Equities | 416 |
| kotak Mahindra Investments | 209 |

Private Wealth, too agrees that a significant quantum of money could rotate into actively managed as well as target maturity debt MFs. However, he added, "Investors can also be expected to switch to NCDs offering relatively higher yields, traditional bonds like perpetual bonds and state-backed bonds for incremental returns to partially offset the higher tax incidence."

Interestingly, while most believe tax-free bonds and debt MFs are most likely to see the shift from MLD money, equity as an option is not being written off.

Amit Jeswani, founder of PMS firm Stallion Asset, says the best bet forward for HNIs would be to move to equity.

"MLDs have been a quasi-equity product, sold with principal protection. Balanced advantage funds, which offer debt + equity returns, are the most similar to MLDs, with taxation similar to equity MFs as well," he said.

He added that fund managers in PMS products are offering "straight-through processing" services, which spread the reinvestment risk over a few months, following which allocation moves to 100% equity.