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Post rate cuts, investors can look at accrual funds

BY [PRASHANT MAHESH](#), ET BUREAU | UPDATED: AUG 02, 2017, 07.55 PM IST

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MUMBAI: After earning double digit returns from fixed income funds over a three year period, investors may need to brace for lower returns in the coming year. Wealth managers and analysts are advising fixed income investors to reduce the proportion of duration funds from their portfolio in favour of accrual funds after the [Reserve Bank of India](#) (RBI), in its policy review meeting on Wednesday, signalled it may not be in a hurry to cut interest rates.

“We are at the fag-end of the rate cut cycle and there could just be one more rate cut,” said Vidya Bala, Head (research), fundsindia.com.

Bala recommends investors to switch from gilt funds—a product that invests in government securities—, which have been top performers in the fixed income category in the last three years, to short term accrual funds such as credit opportunity and corporate bond funds, where the focus is on earning interest income and rate-related risks. She recommends HDFC Medium Term Opportunities Fund and UTI Banking and PSU Fund to fixed income investors with a 1-2 year time frame.

“Investors should position their portfolios towards accrual strategies as no significant rate cuts are expected from here on,” says Vishal Dhawan, Chief Financial Planner, Plan



The RBI, while cutting the repo rate by 25 basis points on Wednesday, maintained its neutral rating

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“The RBI has opted to cut rates, but has maintained a neutral stance of policy – preferring to wait for further data to decide if rates should be further reduced,” says R Sivakumar, Head (Fixed Income), Axis Mutual Fund



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Dhawan recommends investors to raise the proportion of accrual funds in their portfolio to 66 per cent from the earlier 50 per cent, and reduce the proportion of dynamic bond from 34 per cent to 25 per cent. He recommends Birla Sunlife Short term fund and HDFC Medium Term Opportunities fund and in the dynamic fund category recommends IDFC Dynamic Bond Fund.

Accrual funds focus on earning interest income from the coupon offered by bonds they own, while duration funds look at earning income through both capital appreciation when interest rates decline. Though they can earn some returns from capital gains, it is typically small in proportion to their total returns.

In the last three years, investors have earned 10.57 per cent from the Dynamic Bond category, 10.27 per cent from credit opportunities and 11.92 per cent from long term gilt category, as per data from mutual fund tracker Value Research.

Wealth managers advise investors to lower their returns expectation to 7-8.5 per cent as capital appreciation will be lower and investors can now earn returns only from interest accrued on bonds.

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