YOUR MONEY

PSU FUNDS

Recovery may take a while; stay put if you've long horizon

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PSU (public-sector unit) funds, which delivered stellar returns from 2021 to 2024, have underperformed significantly in recent months. These funds have fallen 18.4 per cent on average over the past six months.

Reasons for the slide

The primary reason for this underperformance is over-valuation. Stocks in sectors such as defence, capital goods, railways, and PSU banks had rallied significantly. "Some of them had become extremely expensive. That's why they have corrected heavily in the market correction since September," says Alekh Yadav, head of investment products, Sanctum Wealth.

Some PSU stocks failed to meet market expectations on the earnings front. "Given the exaggerated valuations, the market had started expecting a linear growth in earnings, which did not happen," says Vivek Banka, founder, Goalteller. Profit booking, too, contributed to the fall. "Investors had made a lot of profits in these stocks. Many, therefore, booked profits and exited," says Vishal Dhawan, chief financial planner, Plan Ahead Wealth Advisors.

Key risks and challenges

The performance of PSUs is closely tied to government policies and spending. "In the first half of 2024, government spending fell due to the elections, affecting many of these companies," says Dhawan.

Many PSU businesses are cyclical, making them sensitive to economic slowdowns and reduced consumption. Government ownership also poses challenges. "Many of the government's decisions are driven by its priorities, which may not always be best for the earnings of PSUs," says Dhawan. Capital allocation decisions by the government can also hinder growth. If dividends to the government are prioritised over capital expenditure, these businesses can suffer. Valuations remain a concern even after the recent decline. "If the markets correct further, PSU stocks could continue to decline," says Banka.

Investing in thematic funds like these requires behavioural discipline. "Ideally, investors should have entered these funds when their past returns looked poor. But very few investors would have done that. Most would have entered much later in the rally when PSU fund returns were looking good," says Yadav.

Opportunities in PSU funds

Despite recent setbacks, investing in PSU funds offers certain advantages. "Government-led capital expenditure may rise, benefiting PSUs," says Dhawan. In specific sectors like defence manufacturing, PSUs face limited competition from the private sector, ensuring growth opportunities. PSU banks are cleaning up their balance sheets. "This is in contrast to the rising non-performing assets of non-banking financial companies," says Banka.

Quick recovery is unlikely

The current over-valuation of PSU stocks limits the potential for a quick turnaround. "There is not much scope for an early turnaround in the performance of these stocks. In fact, there may be more downside," says Yadav. Capex announcements in the budget may provide temporary relief to these stocks. But divestment plans, by increasing the supply of PSU papers, could hamper price rise.

What should investors do?

Investors who entered early should book profits as they would be sitting on significant profits. Those who entered the rally late for quick gains should book losses and move to their next bet, as recovery may take time. Those with a 7-10-year horizon may stay put.

STELLAR LONG-TERM RETURNS

These funds have stumbled over the past six months

Funds (Active)	Corpus (₹cr)	Returns (%) 6-mth	1-yr	3-yr	5-yr
ICICI Prudential PSU Equity	2,142.7	-14.0	15.0	NA	NA
Quant PSU	779.6	-22.2	NA	NA	NA
Aditya Birla Sun Life PSU Equity	5,237	-19.1	4.5	27.4	24.3
Invesco India PSU Equity	1,285.8	-20.4	14.2	27.2	24.3
SBI PSU	4,572.1	-16.4	15.2	29.6	22.4
Nifty PSE TRI	NA	-20.1	12.8	33.1	26.6

Returns are for regular, growth plans. Above one-year returns are compound annualised.
Source: Navigation RA

Fixed deposits: Budget FY26 tax incentives may impact interest rates

While the Union Budget 2025-26 may not directly impact interest rates for FDs and RDs, it could influence them through taxation and savings incentives. "Tax benefits under section 80C might be introduced to promote public savings," said Ashish Agrawal, Partner, Dhruva Advisors, a Mumbai-based tax and regulatory services firm.

Factors influencing FD and RD interest rates

RBI monetary policy: Repo rate changes by the Reserve Bank of India directly impact deposit rates, with higher repo rates generally leading to higher returns on deposits.

Inflation: To ensure depositors earn real returns, banks adjust rates based on inflation trends.

Economic conditions and liquidity: In times of economic growth, banks may up deposit rates to attract more funds.

Demand for credit: High demand for loans can push banks to offer better deposit rates to secure funding.

Government policies: Budget announcements can introduce new tax rules that indirectly affect deposit rates.

International interest rates: Global trends can also influence domestic deposit rates, especially for banks with international exposure.

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