PSU, infra and defence mutual funds in spotlight ahead of Budget 2025. Should you invest?

Published on 27th January 2025, By Surbhi Khanna

With the Budget approaching, investors and experts are keeping a close eye on key sectors that are likely to receive a boost from the government. The budget will play an important role in shaping economic priorities, and certain sectors are supposed to benefit from increased allocations, incentives, and reforms. Here's a look at three main sectors that are expected to be in focus and the mutual funds that align with these sectors.

The market experts believe that the key sectors that will remain in focus this Budget will include defence, PSU, and infrastructure. ET Mutual Funds reached out to experts to know what they expect from this budget for these sectors.

Infrastructure sector

The expert believes that this sector is expected to be a focal point in the upcoming budget with a special attention to rural infrastructure and there is also a possibility of initiatives aimed at addressing delays in key infrastructure projects.

"The infrastructure sector is expected to be a focal point in the upcoming Budget, with the government likely to compensate for the reduced expenditure seen this year by allocating higher funds for the next financial year. Special attention is anticipated on rural infrastructure, where additional announcements may be made to address ongoing development requirements. There is also a possibility of initiatives aimed at addressing delays in key infrastructure projects, reflecting the government's commitment to boosting capital investments in this crucial sector," said Abhishek Jain, Head of Research, Arihant Capital Markets.

There were 18 schemes in the category and on an average, they have lost 10.89% since the last budget announcement in July 2024. Though the funds are offering negative returns, the expert recommends that investors should consider increasing their allocation to this space as allocating a reasonable portion of the portfolio can help capture the potential upside.

"The infrastructure sector offers significant opportunities, and investors should consider increasing their allocation to this space. With the government's continued focus on infrastructure and capital goods, this correction presents a good entry point for long-term investments. Allocating a reasonable portion of the portfolio to quality companies in the infrastructure and capital goods sectors can help capture the potential upside as the sector benefits from increased government spending and policy support. A staggered investment approach can also be employed to mitigate risks," advised Abhishek Jain.

PSU funds

The expert believes that this budget will likely place heavy emphasis on PSU divestment, with other measures possibly including reforms in governance, debt restructuring, and transitions to green energy.

"It is likely that this budget will focus heavily on PSU divestment to raise resources, coupled with targeted capital infusion in initiatives like energy, railways, and defence. Other measures may include reforms in governance, debt restructuring, and transitions to green energy. The goal is to improve efficiencies and align PSUs with the country's long-term growth objectives, aiming for a developed India by 2047," said Rajesh Minocha, a Certified Financial Planner (CFP) and founder of Financial.

There were around six funds in the category which on an average basis lost 15.58% since the last Budget announcement in July 2024. With the category offering negative return, the expert advises investors to offload and reduce their exposure, but not to panic. Instead, they should remain cautious. It is important to avoid overexposure to a single theme or sector, and PSU funds should be considered as part of a balanced portfolio. Additionally, investors should monitor budget announcements for potential opportunities and risks.

“For those continuing to invest in PSU funds, there is no need to panic, but investors should remain cautious. While PSUs are integral to India's economic growth, their performance is often tied to government policies and market dynamics. Diversification is key; avoid overexposure to a single sector or theme. Consider holding PSU funds as part of a balanced portfolio and monitor budget announcements for opportunities or risks. Long-term investors should focus on quality PSUs with strong fundamentals,” said Minocha.

Defence funds

For the defence funds, the government's focus in this budget will be to improve consumption rather than capex. Also, India’s defence spending in the last 10 years has increased at a rapid pace compared to global average so investors may wait for valuation to come down, he adds.

“Currently in India consumption is showing a downtrend, so the government's focus during the budget is likely to be more on improving consumption. The Ministry of Defence recently announced a Rs 21,700 crore work clearance, emphasizing its commitment to reform and modernization. The focus is on capability building in areas such as robotics, AI, training, and simulation, alongside fast-tracking key projects. Trump is expected to strengthen military capabilities through procurement or strategic alliances,” said Vishal Dhawan, CEO, Plan Ahead Wealth Advisors, a wealth management firm in Mumbai.

“India’s defense spending in the last 10 years has increased at a rapid pace (10%) than the global average (3%). Investors may want to wait for more valuation comfort before they allocate funds, and when the valuations are more reasonable, have a long-term investment horizon,” he adds.

There were two funds in the category. Motilal Oswal Nifty India Defence Index Fund lost the most at around 15.35% since the last Budget announcement. HDFC Defence Fund lost 12.19% during the same period.

Now the funds based on the defence sector are offering negative returns, therefore the expert advises that investors should continue to hold their investments as the long-term outlook for the sector remains positive.

“The long-term outlook for the defence sector remains positive, supported by increasing government spending and strategic initiatives. Global geopolitical tensions and India’s rising focus on self-reliance are fuelling order flow and revenue growth for domestic Defence companies,” said Dhawan.

“A robust order book could drive revenue growth. By mandating higher procurement from local suppliers, the share of domestic procurement has increased from 55% in 2019 to 75%, with further growth expected in the coming years. However, it is important to keep in mind that high volatility could be encountered along this journey,” he added.

“Despite the recent decline in the Defence Index, its trailing P/E is still nearly double that of the Nifty 500, indicating that valuation comfort remains lacking. So, if an investor is already invested, it's better to stay invested. However, if you're looking to allocate now, it’s advisable to wait for more valuation comfort,” he further added.

One should always make investment decisions based on their risk appetite, investment horizon, and goals.