



## YOUR MONEY

### 2026 OUTLOOK: DEBT MUTUAL FUNDS

# Skip duration bets, stick to shorter and medium-duration funds

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After a phase of policy easing and bond market rallies, debt mutual fund investors are heading into a different environment in 2026. The consensus among experts is that gains from falling interest rates are largely behind us. What lies ahead is a year of relative rate stability.

#### Limited room for rate cuts

The central bank cut the repo rate by 125 basis points in 2025. That phase has largely played out. “Any further cut depends on inflation staying below the target, and some drag on growth,” says Mayur Chauhan, fund manager — fixed income, Quantum AMC.

The Reserve Bank of India (RBI) expects inflation to move closer to 4 per cent in the first half of FY26. “There may be one final rate cut on February 6, but the probability is less than 50 per

cent,” says Joydeep Sen, independent debt market expert.

#### Duration bets are best avoided

With the rate-cut cycle now at or near its end, increasing exposure to long-duration funds does not make sense for most investors. “Build a large part of the portfolio in lower-duration securities and rely on the accrual theme in 2026,” says

Devang Shah, head of fixed income, Axis Mutual Fund.

Markets could start pricing in the next phase of the cycle, which could include rate hikes from 2027. Any such shift would hurt longer-maturity bonds more sharply.

The rupee has been under pressure. “In such periods, short-term interest-rate bets tend to become riskier,” says Vishal Dhawan, founder and CEO, Plan Ahead Wealth Advisors.

For investors who might still consider long-duration funds, the investment horizon becomes critical. “The holding period should broadly match the portfolio maturity of the fund. A fund with a 10-year maturity profile requires an eight-to-10-year horizon,” says Sen.

#### Medium-duration funds: Selective opportunity

Medium-duration funds occupy the four-to-six-year maturity segment and offer a balance between return potential and interest-rate risk. Yields in this

segment are typically higher than in the shorter-duration segment, which improves return potential. Chauhan points out that medium-duration funds are for investors who can take some risk. If yields rise, mark-to-market losses would follow.

Sen suggests that investors align their holding period with these funds’ maturity profile, staying invested for four to six years.

#### Short-duration funds: Core holdings

Shorter-duration funds are well-suited to the current environment. Their returns rely primarily on accrual income, and they are less susceptible to mark-to-market volatility in case interest rates rise.

These funds are appropriate for investors with six months to one-year horizon. “If liquidity infusion continues, as is possible, investors in shorter-duration funds would benefit,” says Dhawan.

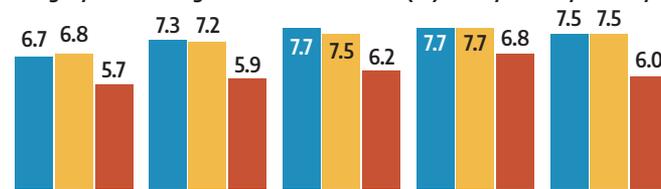
#### Where to invest

For a horizon of around two years, Shah suggests opting for income-plus arbitrage fund-of-funds, which offers tax efficiency to investors in higher tax slabs.

Horizon matching remains the most important principle. “Ultra-short and low-duration funds are suited for a horizon of less than one year; medium-duration and corporate bond funds are appropriate for three-to-five-years; while long-duration funds are suited for those who want to make a long-term allocation,” says Sen.

## Recent performance trends

Category-wise average returns in debt funds (%) ■ 1-yr ■ 3-yr ■ 5-yr



Returns are of direct plans; Returns above one-year are annualised  
Source: PBCS.in