



RISK APPETITE AMONGST DEBT FUND MANAGERS RISES marginally

Contacts:

Karthik Srinivasan
karthiks@icraindia.com
+91-22-3047 0028

Nikhil Rungta
nikhilar@icraindia.com
+91-22-3047 0020

Ravi Mittal
ravim@icraindia.com
+91-22-3047 0036

ICRA has ratings outstanding on 80 liquid/debt mutual fund schemes across 22 Asset Management Companies (AMCs) as on date. The analysis of the credit quality across the ICRA rated schemes reveals that majority of the schemes continue to qualify comfortably for the highest rating levels within their respective maturity categories. Of the three schemes that ICRA had downgraded in March 2009, one has been upgraded to the earlier rating level in third quarter of FY2009-10 while the rating on others have been retained.

In the past few months, we are witnessing a relatively higher propensity of the fund managers to invest in securities of companies that would have a long term credit rating of less than "LAA" or equivalent rating category as a means to improve the returns especially on the flagship liquid and ultra short term schemes. However over 90% of the exposure across ICRA rated Mutual Fund schemes continues to remain in better rated (generally entities with long term rating of LAA and above) entities alleviating credit related concerns, if any.

The assets under management (AUM) of ICRA rated debt schemes continue to remain at elevated levels which could be attributed to banks and other institutional investors parking their surplus funds in mutual funds consequent to the low credit off-take in the nine-month period ended December 2009. Corporate sector too favour investing in liquid / ultra short term and debt schemes as part of their cash management strategy as these schemes offer superior returns (relative to short term deposit rates) while maintaining sound credit quality of the investment portfolio.

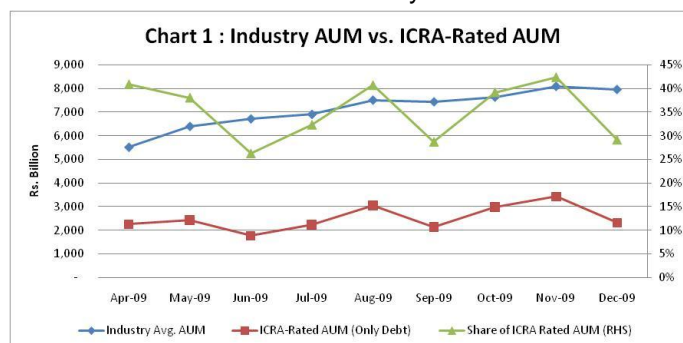
The rise in the AUM of the ICRA rated schemes during the last couple of quarters was led primarily by sharp rise in the size of Ultra Short Term (formerly Liquid Plus) schemes. With SEBI lowering the maximum maturity of investments in liquid schemes to ninety days and expectations of a likely reversal in the yield curve by the year end, the residual maturity across the ICRA rated schemes continue to decline except for brief periods wherein the fund managers take a short-term directional view on interest rates.

Notwithstanding the increase in AUM of ICRA rated debt mutual funds, the high proportion of incremental investments - largely in Government Securities and highly rated Banks – continue to support the overall credit quality of these schemes.

Website:
www.icra.in

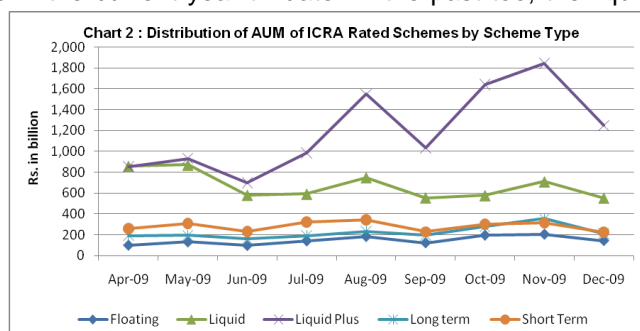
Industry AUM increases in YTFY10 amidst rising liquidity and buoyant capital markets; declines in Dec-09 on withdrawal of funds by wholesale investors...

ICRA has ratings outstanding on 80 liquid / debt mutual fund schemes across 22 Asset Management Companies (AMCs). These schemes account for nearly 30% of the industry's average Assets under Management (AUM) during December 2009¹. If one were to consider only the debt mutual fund schemes (excluding equity schemes and Fixed Maturity Plans)² of the industry, ICRA market share would be around 50%. The AUM of ICRA rated liquid/debt schemes which stood at Rs. 2.2 trillion as on Apr-09 increased to Rs. 3.4 trillion as on Nov-09 supported by higher systemic liquidity and rise in banks investments in mutual fund during the period. However, with the quarter end redemption pressure driven by advance tax payments, quarter end balance sheet management by institutional investors coupled with the RBI voicing its discomfort on banks parking their surplus with Mutual funds guideline led to a decline in the industry AUM in debt schemes during December 2009. Accordingly, the AUM of ICRA rated schemes too witnessed a decline and stood at around Rs. 2.4 trillion as of December 31, 2009. While some uptrend could be observed in January 2010 in the AUM of debt schemes, it would be constrained by the pick up in bank credit and banks limited willingness to park their surpluses in mutual fund schemes post RBI's views on such investments.



Ultra Short maturity schemes: a clear favourite with investors

In the last few months, the growth in debt AUM is largely driven by the rise in AUM in the ultra short term (formerly liquid plus) schemes. The sharp growth was supported by ample liquidity in the banking system and a significantly lower credit off-take in the current year till date. In the past too, the liquid and ultra short term schemes had higher AUMs as banks and corporate houses used to park their surplus funds here for short durations as part of cash flow management strategy. As a result, among the ICRA rated schemes, the investments in liquid and ultra short term schemes continues to remain high at around 75% of the overall AUM as on December 31, 2009. Since SEBI issued guidelines on capping the final maturity on investments made by liquid schemes, investors have been moving their investments from liquid schemes to the ultra short term funds, which has no such tight restrictions and the liquidity profile is fairly comfortable in addition to providing them with higher returns. Thus barring the quarter ending periods, the AUM of the ultra short term funds continues to remain robust in the current financial year. However, recent SEBI's guideline to value money market and debt securities with maturities over 91 days may result in higher volatility of return for such schemes and may slightly impact its attractiveness to the investors.

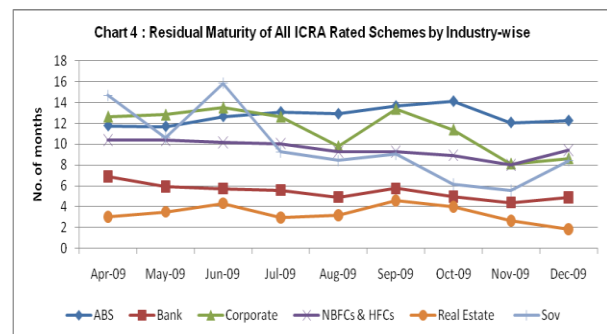
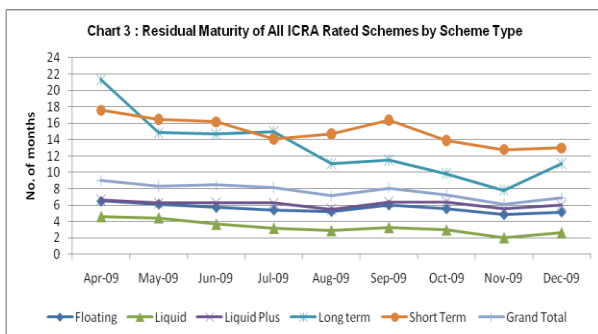


¹ Source: www.amfiindia.com & ICRA research

² Anecdotal evidence suggests AUM under equity schemes and FMP schemes are close to 30% and 5% respectively of the average Industry AUM as on December 2009

Residual maturity profile declines further in last six months

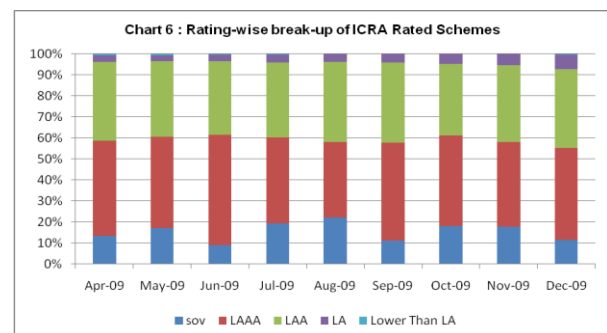
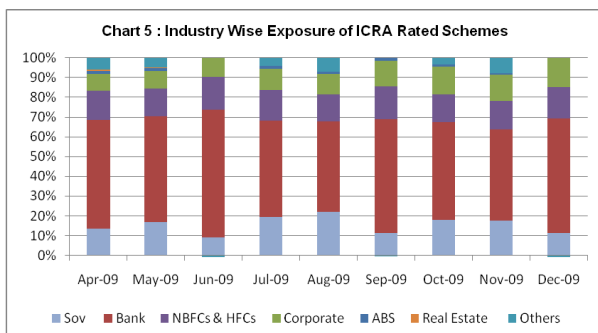
While the maturity profile for liquid schemes have declined in the last few quarters³ in line with the SEBI guidelines on cap on the maximum tenure of the underlying investments, the residual maturity for other ICRA rated schemes have also come down in the same period in line with investors investment time horizon and fund managers views on interest rates.



With the rise in AUMs of liquid and other short term schemes, the fund managers have been increasing their preference for short duration papers. The ample liquidity in the banking system, the low credit off-take and expectations of possible hardening of interest rates in the short term have been influencing the fund managers’ decision to remain invested largely in short duration papers. A similar trend is found if one analyses the maturity profiles of the underlying investments with break-up being rating-wise or asset class-wise. The small rise in the residual maturity profile of the schemes during the quarter end is primarily on account of the redemption pressures during those periods wherein the fund managers liquidate the overnight investments and other very short term investments to reduce the impact on the net asset values.

Risk appetite increasing marginally across debt mutual fund schemes...

On the back of high systemic liquidity leading to a sharp fall in the overnight money market and short term rates, fund managers have been struggling to give higher returns in the flagship (ultra short term) schemes. Supported by improving corporate earnings in last two quarters and signs of economy reviving, fund managers are now willing to increase their exposure to corporate and NBFC sector wherein the yields are better than those available on Government Securities and Bank certificate of deposits and term deposits. The increase in risk bearing ability is also seen from the sector wise analysis of the schemes investments. The incremental investments have been made primarily in the banks, non-banking financial companies and corporate sector. The share of investments in corporate securities as a percentage of total AUM increased to 14.69% as on Dec-09 compared to 8.26% as on Apr-09. At the same time, the fund houses have practically stayed away from investing in sensitive sectors such as real estate during the same period. Consequently, the exposure to the real estate segment has declined from about 0.50% of the AUM as on April 2009 to 0.11% as on December 2009. Similarly the exposure to the securitised debt (Asset backed Securitised papers) has also been coming down and is less than 1% of the AUM with little incremental investments made by ICRA rated schemes in such papers.



Out of the 80 ICRA rated schemes, twenty eight schemes had exposures to ABS and / or real estate papers, but as of December 2009, the number of such schemes has reduced to just sixteen. Also as of December 2009, only five schemes have exposure to real estate sector.

³ Except in the month of Dec-09, wherein, to meet the quarter-end redemption pressure, fund managers liquidated investments in Government Securities (including CBLO investments) and other short duration papers which led to the rise in residual maturity.

In case we were to analyse scheme type-wise, the exposure to real estate and ABS papers have been less than 0.15% and 0.90% respectively as on December 2009. For some individual schemes, the proportion is marginally higher, but we do not see any further rating pressures as such exposures are running down and fresh investments, if any, are being done only in highly rated papers.

In addition, we are witnessing a relatively higher propensity of the fund managers to invest in securities of companies that would have a long term credit rating of less than "LAA" or equivalent rating category. Corporate have also been raising funds from Mutual Funds as they are able to borrow at lower rates as compared to bank borrowings. ICRA analysis shows share of entities with a long term rating of LAAA⁴ and Government Securities has been declining and stood at 55.2% as on Dec-09 compared to 60.5% as on May-09. On the other hand that the overall exposure to the lower rated entities has been increasing over the past few months with LA and lower rated entities standing at 7.3% as on Dec-09 compared to 3.4% as on May-09. However comfort can be derived that such exposures account for a small portion of the total AUM, alleviating any concerns on the credit quality of the ICRA rated schemes. A similar inference can be drawn if we were to analyse the portfolio of various schemes by scheme type and is given in the Annexure.

... But credit quality of ICRA rated mutual fund schemes remain comfortable

The analysis of the credit quality across the ICRA rated schemes reveals that 75 schemes out of the 80 schemes rated by ICRA continue to qualify comfortably for the highest rating levels of mfAAA (schemes having residual weighted average maturity of greater than 12 months) and mfA1+ (schemes with a residual average maturity of less than 12 months). Of the remaining schemes, ratings on two schemes were downgraded from the highest rating levels for deterioration in portfolio credit quality while the balance three schemes were not accorded the highest ratings in the first instance on account of their underlying investment portfolios.

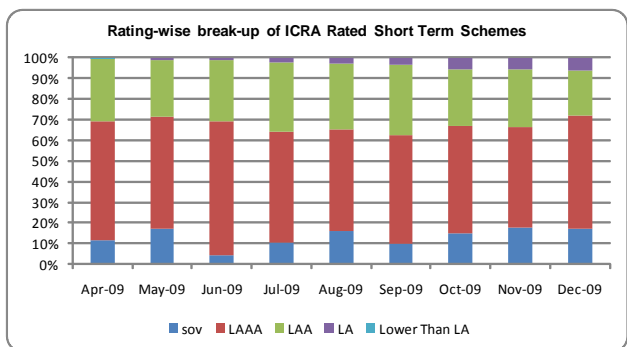
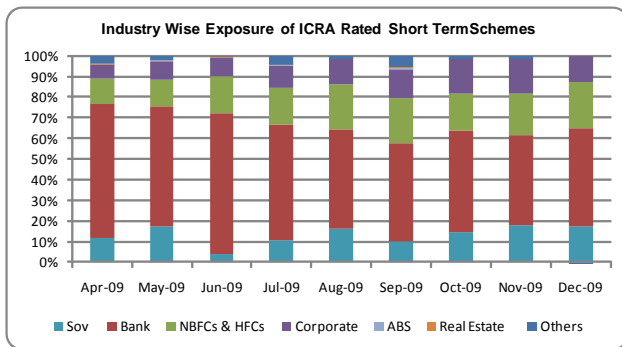
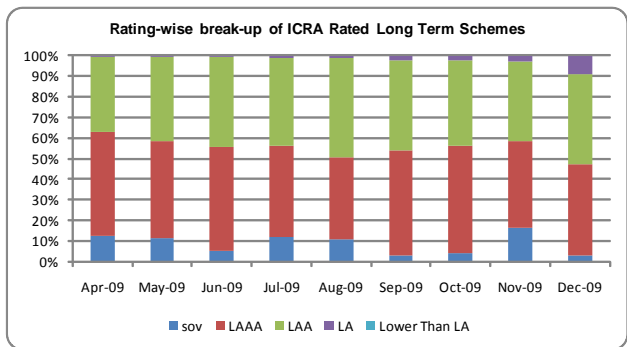
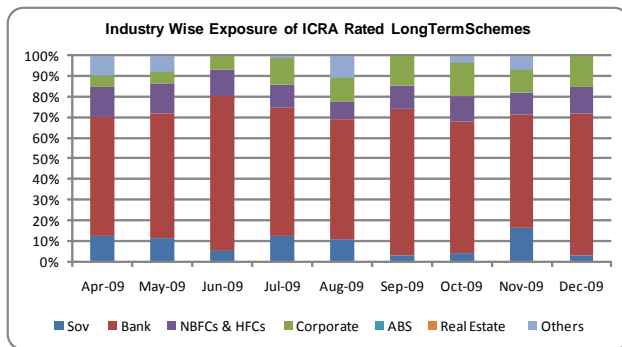
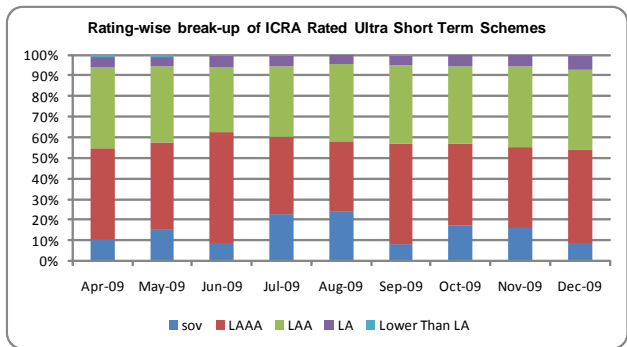
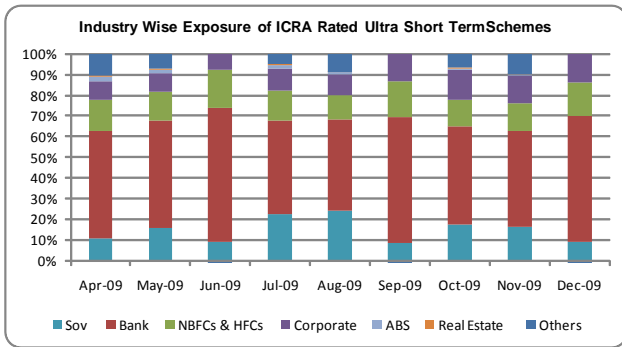
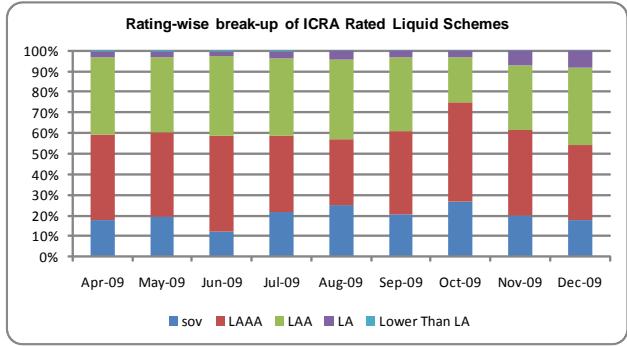
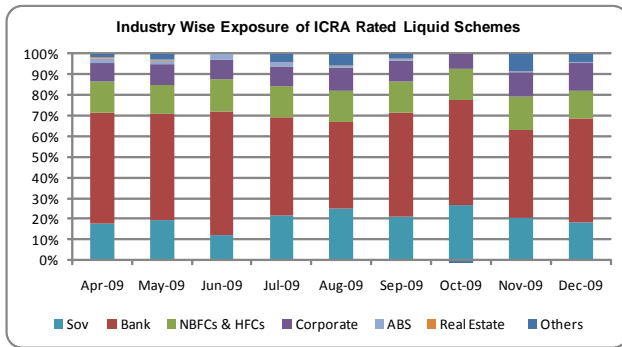
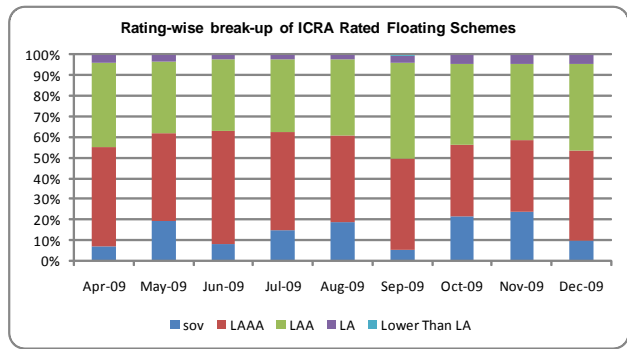
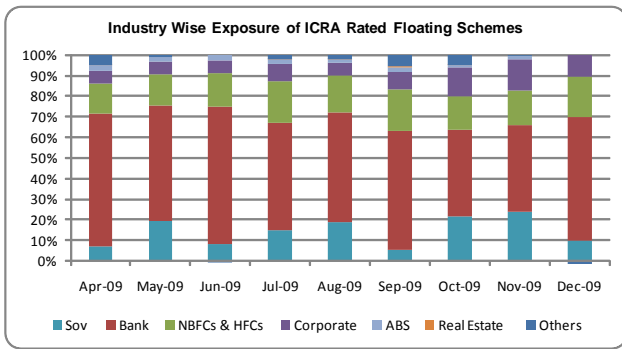
Overall Comments

The AUM of the ICRA rated debt schemes continue to grow on the back of excess liquidity in the banking system and investors quest for better post tax returns. However further growth in the debt AUM would depend on market conditions, banks limited willingness to park their surpluses in mutual fund schemes post RBI's views on such investments and expectations of pick up in bank credit in the current quarter. While we are witnessing a relatively higher propensity of the fund managers to invest in securities of companies that would have a long term credit rating of less than "LAA" or equivalent rating category as a means to improve the returns especially on the flagship liquid and ultra short term schemes, the high proportion of incremental investments that continue in Government Securities and highly rated Banks supports the overall credit quality of these schemes.

February 2010

⁴ ICRA takes the long term view on the credit quality of underlying entities in its analysis of credit quality of mutual fund schemes.

Annexure 1: Industry-Wise and Rating-Wise exposure of ICRA Rated Schemes



Annexure 2: List of ICRA rated schemes with Credit Quality Ratings as on January 31, 2010.

Scheme	Rating
AIG Short Term Fund	mfAAA
Axis Liquid Fund	mfA1+
Axis Treasury Advantage Fund	mfA1+
Axis Short Term Fund	mfAAA
Baroda Pioneer PSU Bond Fund	mfAAA
Baroda Pioneer Liquid Fund	mfA1+
Baroda Pioneer Treasury Advantage	mfA1+
Birla Sun Life Cash Plus	mfA1+
Birla Sun Life Floating Rate - Long-Term Plan	mfAAA
Birla Sun Life Floating Rate - Short-Term Plan	mfAAA
Canara Robeco Liquid Fund (formerly Canliquid Fund)	mfA1+
Canara Robeco Dynamic Bond Fund	mfAAA
Canara Robeco Short Term Fund	mfA1+
Canara Robeco Floating Rate Fund (formerly Canfloating Rate Fund)	mfA1+
Canara Robeco Liquid Plus Scheme (formerly Can Liquidplus Scheme)	mfAAA
DSP BlackRock Strategic Bond Fund	mfAAA
DSP BlackRock Money Manager Fund	mfAAA
Fidelity Cash Fund	mfA1+
Fidelity Ultra Short Term Debt Fund	mfA1+
Fidelity Flexi Bond Fund	mfAAA
HDFC 36M FMP 2007	mfAA
HDFC Cash Management Fund – Savings Plan	mfA1+
HDFC Cash Management Fund-savings Plus plan	mfAAA
HDFC Floating Rate Income Fund - Short-Term Plan	mfA1+
HDFC High Interest Fund - Short Term Plan	mfAAA
HDFC Liquid Fund	mfA1+
HDFC Quarterly Interval Fund - Plan A	mfA1+
HDFC Quarterly Interval Fund - Plan B	mfA1+
HDFC Quarterly Interval Fund - Plan C	mfA1+
HDFC Short Term Plan	mfAAA
HSBC Cash Fund	mfA1+
HSBC Flexi Debt Fund	mfAAA
HSBC Floating Rate Fund – Long-Term Plan	mfAAA
HSBC Floating Rate Fund – Short-Term Plan	mfAAA
HSBC Ultra Short Term Bond Fund	mfA1
HSBC Income Fund- Short Term Plan	mfAAA
ICICI Prudential Fixed Maturity Plan – Series 49 – Three Years Plan A	mfAA
IDFC Cash Fund	mfA1+
IDFC Liquid Plus Treasury Fund	mfA1+
IDFC Liquid Plus Investment Fund	mfAAA
Kotak Bond ShortTerm Plan	mfAAA
Kotak Flexi Debt Scheme	mfAA+
Kotak Floater Long Term Scheme (K-FLT)	mfAAA
LICMF Income Plus Fund	mfA1
LICMF Liquid	mfA1+
Mirae Asset Liquid Fund	mfA1+
Mirae Asset Ultra Short Term Bond Fund	mfA1+
Morgan Stanley Active Bond Fund	mfAAA
Morgan Stanley Short-Term Bond Fund	mfAAA
Principal Ultra Short Term Fund	mfA1+
Principal Floating Rate Fund - Short Maturity Plan	mfA1+

Scheme	Rating
Principal Floating Rate Fund - Flexible Maturity Plan	mfAAA
Principal Income Fund	mfAAA
Principal Cash Management Fund - Liquid Option	mfA1+
Principal Income Fund - Short Term Plan	mfAAA
Reliance Liquid Fund – Treasury Plan	mfA1+
Reliance Floating Rate Fund	mfAAA
Reliance Liquidity Fund	mfA1+
Reliance Money Manager Fund	mfA1+
Reliance Short Term Fund	mfAAA
Reliance Medium Term Fund	mfAAA
SBI Short Horizon Fund - Ultra Short Term Fund	mfA1+
SBI Magnum Insta cash Fund	mfA1+
SBI Magnum Premier Liquid Fund	mfA1+
Shinsei Liquid Fund	mfA1+
Shinsei PSU Bond Fund – Ultra Short Term Plan	mfA1+
Shinsei Treasury Advantage Fund	mfA1+
Tata Floater Fund	mfAAA
Tata Floating Rate Short Term Fund	mfAAA
Tata Income Fund	mfAAA
Tata Liquid Fund	mfA1+
Tata Liquidity Management Fund	mfA1+
Tata Short Term Bond Fund	mfAAA
Tata Treasury Manager Fund	mfAAA
Templeton India Treasury Management Account	mfA1+
Templeton India Ultra Short Bond Fundt	mfA1+
Templeton Floating Rate Income Fund – Short Term Plan	mfA1+
UTI Floating Rate – Short Term Plan	mfAAA
UTI Liquid Fund Cash Plan	mfA1+
UTI-Treasury Advantage Fund (UTI Liquid Plus Scheme)	mfAAA

Annexure 3: Scheme-wise break-up of ICRA Rated Schemes as on January 31, 2010

Fund House	Type of Schemes						Total
	Liquid	Ultra Short	Short Term	Long Term	Floating	FMP	
AIG MF			1				1
Axis MF	1	1	1				3
Baroda Pioneer MF	1	1		1			3
Birla Sunlife MF	1				2		3
Canara Robeco MF	1	1	1	1	1		5
DSP Blackrock MF		1		1			2
Fidelity MF	1	1		1			3
HDFC MF	2	1	5		1	1	10
HSBC MF	1	1	1	1	2		6
ICICI Prudential MF						1	1
IDFC MF	1	2					3
Kotak Mahindra MF			2	1			3
LIC MF	1	1					2
Mirae MF	1	1					2
Morgan Stanley MF			1	1			2
Principal MF	1	1	1	1	2		6
Reliance MF	2	1	2		1		6
SBI MF	2	1					3
Shinsei MF	1	1	1				3
Tata MF	1	2	1	2	1		7
Franklin Templeton MF	1	1			1		3
UTI MF	1	1			1		3
Total	20	19	17	10	12	2	80



ICRA Limited

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CORPORATE OFFICE

Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002

Tel: +91 124 4545300; Fax: +91 124 4545350

Email: info@icraindia.com, Website: www.icra.in

REGISTERED OFFICE

1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001

Tel: +91 11 23357940-50; Fax: +91 11 23357014

Branches: **Mumbai**: Tel.: + (91 22) 24331046/53/62/74/86/87, Fax: + (91 22) 2433 1390 **Chennai**: Tel + (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294, Fax + (91 44) 2434 3663 **Kolkata**: Tel + (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008, Fax + (91 33) 2287 0728 **Bangalore**: Tel + (91 80) 2559 7401/4049 Fax + (91 80) 559 4065 **Ahmedabad**: Tel + (91 79) 2658 4924/5049/2008, Fax + (91 79) 2658 4924 **Hyderabad**: Tel +(91 40) 2373 5061/7251, Fax + (91 40) 2373 5152 **Pune**: Tel + (91 20) 2552 0194/95/96, Fax + (91 20) 553 9231

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