

May 2016

L&T Income Opportunities Fund

The government's commitment to maintain fiscal prudence, sustained low inflation and expectation of normal monsoon this year has led to softening of yields over the past few months. Reserve Bank of India (RBI) in its monetary policy on 5th April 2016 lowered the repo rate by 25 bps at 6.50% and continued to maintain an accommodative policy stance, keeping a close watch on macroeconomic and financial developments in the months ahead. While the RBI may still provide more rate cuts over short term, quantum of it over long term may be limited considering various other factors like – pickup in economic growth, RBI's inflation targeting framework, global factors etc. In that context, while an investor may enjoy a duration rally over short term in a typical bond fund, he could get stuck at low yielding portfolio over medium to longer term. In such a scenario, **L&T Income Opportunities Fund (LTIOF)** with its yield oriented strategy could be an appropriate investment option for medium to long term investors looking for relatively higher yielding portfolio. In this edition of **Fund Insights**, we discuss the fund's investment approach, portfolio positioning and further highlight the key benefits of investing in this fund.

Investment approach

L&T Income Opportunities fund is a bond fund which focuses on accrual based yield enhancement strategy by taking measured exposure to well researched and mispriced credits. The Fund Manager intends to construct a portfolio with a relatively higher yield compared to high credit quality bond funds without assuming significant interest rate risk as the portfolio average maturity is restricted to 3 years. Fund's credit selection is based on internal rigorous credit research process of assigning internal credit ratings encompassing detailed analysis of financial strength, liquidity, management track record, corporate governance and interactions with management, competitors, vendors and various other intermediaries. The overall portfolio approach aims to maximize the risk adjusted returns by investing in good quality high yielding companies.

Key Attributes of L&T Income Opportunities Fund

A strategy that can:

- *Yield oriented fund which aims to strike a good balance between risk and return*
- *Own securities which provide adequate yield pick-up over G-Sec*
- *Positioned at the short to medium end of the yield curve to avoid undue interest rate risk*
- *Offer tax efficient returns*

L&T Income Opportunities Fund

Moderate duration risk

Average Maturity not to exceed 3 years

High portfolio yield

A high-yielding, accrual oriented strategy for the medium term investors

Well Researched Credits

Rigorous internal credit research process to spot mispriced credits

Tax efficient

A well differentiated investment strategy, which can be held as a core holding, allows investors to stay invested for over 3 years to earn better post tax returns

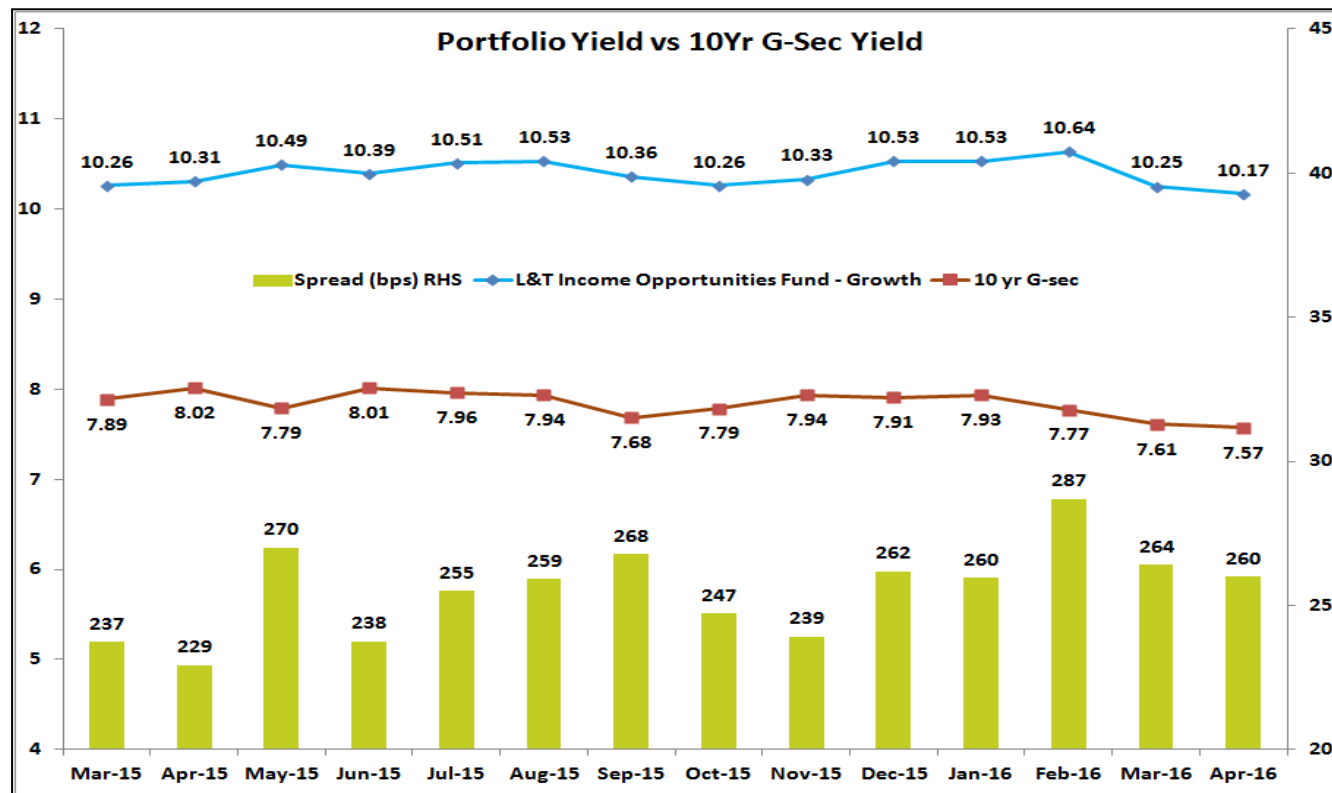
Stable investor base

Exit load for 1 years to ensure stability of flows / avoid abrupt flows which can impact existing investors

Key Benefits

1. Portfolio yield pick-up over G-sec and duration fund portfolios

The fund aims to construct a portfolio with significant yield pick-up over g-sec and duration fund portfolios. The chart below shows the portfolio yield of LTIOF against the 10-yr g-sec yield. On an average, LTIOF has been able to maintain a positive yield spread of 225-250 bps over g-sec. As of 29-April-2016, the portfolio yield was 10.17% which is about 260 bps higher than 10-yr g-sec. This could be attractive for investors looking to make allocation to bond funds with over 3 year investment horizon.



Source: ICRA MFIE, Bloomberg. Data as on April 2016

2. *Strong focus on credit selection*

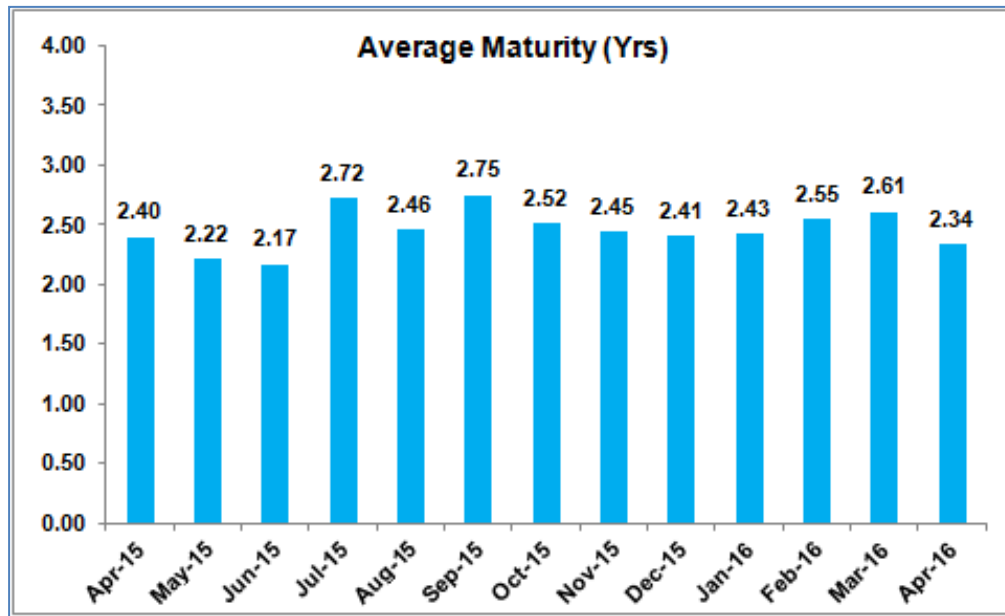
The fund has a rigorous credit selection process to spot mispriced credit opportunities. The focus is on yield enhancement through measured exposure to such well researched and mispriced credits. The fund follows an accrual based strategy and has a relatively low portfolio turnover. As at April 2016 end, the scheme had predominantly invested in a combination of AAA and equivalent (42.9%) and AA- and above rated securities (40.8%). The Fund has consistently maintained a moderate exposure to select A / A+ and equivalent rated securities for seeking attractive yields given their risk profile. As at April 2016 end, the scheme had 16.2% exposure to A / A+ rated companies.

Portfolio Date	A/A+ and equivalent	AA/AA+ and equivalent	AAA and equivalent
Apr-16	16.23	40.87	42.90
Mar-16	14.76	43.81	41.43
Feb-16	13.22	42.18	44.60
Jan-16	13.56	39.15	47.28
Dec-15	14.19	38.80	47.01
Nov-15	14.50	42.56	42.95
Oct-15	19.16	48.83	32.01
Sep-15	19.66	53.51	26.83

Source: ICRA MFIE. Data as on April 2016)

3. *Low to moderate interest rate risk*

L&T Income Opportunities Fund does not take undue interest rate risk and the portfolio average maturity of the Fund is capped at 3 years. As a result the predominant portion of the fund’s return is expected to come from yield accrual with some potential for capital gains in a favorable interest rate environment. The fund’s portfolio average maturity as at the end of April 2016 was 2.34 years.



(Source: ICRA MFIE. Data as on April 2016)

Brief details about the current key holdings in the portfolio (as at April 2016)

Issuer	Rating	Description
Intime Properties Limited	AAA(SO) by Fitch	It is a commercial mortgaged backed security (CMBS) with structured cash flows in the form of pre-agreed monthly lease rentals which largely comes from Fortune 500 companies like Qualcomm, Accenture, Bank of America, Deloitte, HSBC, etc. It is a part of K Raheja Group and owns completely constructed & fully operational 3 commercial towers in Hyderabad which are more than 99.5% occupied with long term lease agreements with corporates. No construction risk. No price/demand risk. In terms of instrument characteristics, CMBS is very similar to Lease Rental Discounting with high visibility on cash flows.

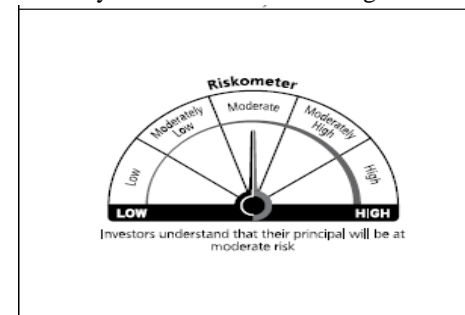
Sunny View Properties Ltd	AA(SO) by ICRA	This is a structured paper with an un-conditional / irrevocable / continuing Debt Servicing Reserve Account (DSRA) guarantee from its parent, Shapoorji Pallonji Company Ltd (SPCL). SPCL is a flagship holding company of Shapoorji Pallonji Group which has its business interests in construction business on its own books and businesses like contracting, water purification, infrastructure development, solar power generation etc undertaken through various subsidiaries. The SP Group is also the largest private shareholder (with an 18.37% stake) in Tata Sons Limited, the holding company of the Tata Group.
Business Broadcast News Holdings Limited	AAA(SO) by CARE	No credit risk on the underlying company. This exposure is fully backed by Reliance Capital Ltd's un-conditional, irrevocable, continuing and 100% corporate guarantee, backed by Board Resolution. BBNHL is Reliance Capital Ltd's investment vehicle which owns and operates Bloomberg TV in India. Reliance Capital Ltd is one of the most diversified financial conglomerates with established presence across lending business, mutual funds, life insurance & general insurance etc. Fifth largest Life Insurance player in private sector. Fifth largest General Insurance player in private sector. Leading NBFC with loan book ~ Rs 20,000 cr. Under control asset quality, with GNPA% at 2.8% as on Jun-15. Amongst the top 3 Mutual funds in India. High capital levels with capital adequacy ~24%.
Future Retail Ltd	AA- by CARE	One of the largest retail business operators in the country with strong brand recognition (Big Bazaar, Food Bazaar, FBB etc). High sales turnover in the value segment of retail business provides comfort. Merger with Bharti Retail, which is fully equity funded, will provide further scale to business. It has presence across retail value chain from procurement, supply chain management to retail stores. Diversification across product range (groceries, apparel, general merchandise, home furniture, electronics etc) as well as geographical (more than 95 cities) presence. Healthy operating margins, on improving trajectory. Improved credit metrics as it raised equity of ~Rs.1,900 cr in FY15 which has lead to improvement in liquidity profile as well as debt reduction. Significant value on the underlying investments (Insurance, supply chain) made by the company provides further financial flexibility. Strong covenants related to debt reduction and rating downgrade built into the deal to protect the debt holder's interest

In Summary

L&T Income Opportunities Fund being a yield focused funds with moderate duration exposure could be an appropriate investment alternative for strategic allocation. The fund with its careful credit selection strategy offering attractive yield pickup could potentially deliver better risk adjusted performance over medium to long term. Relatively steady nature of the fund coupled with fund manager’s ability to own higher yielding securities make it a suitable fixed income investment option for investors looking to hold onto their investments for more than 3 year period to avail tax benefit.

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L&T Income Opportunities Fund - An open-ended income scheme: • Generation of regular returns and capital appreciation over medium to long term • Investment in debt instruments(including securitized debt), government and money market securities



Mutual Fund investments are subject to market risks, read all scheme related documents carefully.